No. 95-301 AUG 17 1995

OFFICE OF THE CLERK

In The

SUPREME COURT
OF THE UNITED STATES
October Term, 1995

STONEHENGE INSURED NOTES-I LIMITED PARTNERSHIP; AND HARBISON-FISCHER MFG. CO., INC., *Petitioners*,

v.

UNITED STATES DEPARTMENT OF THE TREASURY, STATE OF NEW YORK, and PHILIP ZINKE, *Respondents*.

Petition for a Writ of Certiorari
to the United States Court of Appeals
for the Second Circuit

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PETITIONERS
August 1995

QUESTIONS PRESENTED

1. Whether an admitted fiduciary under ERISA who admittedly self-deals with ERISA plan assets, may avoid liability because the ERISA plan beneficiaries do not meet a burden of proof imposed by the trial court, to trace the plan assets for purposes of imposing the equitable remedies of restitution and constructive trust.

2. Whether an investment manager who admits he is an ERISA fiduciary to ERISA plans and their affiliated entities (limited partnership) has the burden of proof to justify his admitted self-dealing with plan assets.

3. Whether ERISA plans and their affiliated entities (limited partnership) have the burden of proof under ERISA to show tracing of assets for imposition for the equitable remedies of restitution and constructive trust, despite admitted self-dealing with plan assets by an admitted fiduciary.

4. Whether an admitted ERISA fiduciary is liable as a non-fiduciary under ERISA for equitable remedies of restitution and constructive trust for a knowing breach of the ERISA prohibition against self-dealing.

5. Whether an admitted ERISA fiduciary may terminate his fiduciary relationship to an ERISA plan and its affiliates without an express unambiguous communication to the ERISA plan or its affiliates.

LIST OF PARTIES

Petitioner, Stonehenge Insured Notes-I Limited Partnership

Petitioner Harbison-Fischer Manufacturing Co., Inc., is a wholly-owned subsidiary of Harbison-Fischer, Inc., a Delaware corporation

The United States Department of the Treasury

The State of New York

Respondent Philip W. Zinke wholly defaulted in the lower court proceedings, but appeared at trial in the bankruptcy court.

Judith A. Zinke, Goodman Plumbing and Heating Corp., Robert Abrusso, Strazzen & Son, Environmental Control Board, V.A. Paradise, and John and Jane Does no longer have an interest in the outcome of the petition for certiorari

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IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1995

STONEHENGE INSURED NOTES-I LIMITED PARTNERSHIP; AND HARBISON-FISCHER MFG. CO., INC., *Petitioners*,

v.

UNITED STATES DEPARTMENT OF THE TREASURY, STATE OF NEW YORK, and PHILIP ZINKE, *Respondents*.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

---

Stonehenge Insured Notes-I Limited Partnership, and Harbison-Fischer Mfg. Co., Inc., respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, B-1) is unreported. The opinions of the district court (App., *infra*, C-1, D-1) are unreported. The Findings of

Fact and Conclusions of Law of the bankruptcy court (App., *infra*, F-1) are unreported. The opinion of the bankruptcy court on the Motion for New Trial (See App., *infra*, E-1) is reported at 149 Bankr. Rptr. 310 (E.D.N.Y.1992).

JURISDICTION

The court of appeals entered its judgment on January 10, 1995 (App., *infra*, B-1). The court of appeals denied a timely filed Motion for Rehearing with Suggestion for Rehearing *In Banc* on May 19, 1995 (App., *infra*, A-1). The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

STATUTORY PROVISIONS INVOLVED

29 U.S.C. §1002(21)(A) provides that

> A person is a fiduciary with respect to a plan to the extent
>
> (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets,
>
> (ii) he rendered investment advise for a fee or other compensation, direct or indirect, with respect to any monies or other property of such plan, or has any authority or responsibility to do so, or

(iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.

29 U.S.C. §1104(a) 29 U.S.C. Sec. 1104(a), provides in relevant part:

(1) ... [A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and--

(A) for the exclusive purpose of: (i) providing benefits to participants and their beneficiaries; and (ii) defraying reasonable expenses of administering the plan;

(B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;

(C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and

(D) in accordance with the documents and instruments governing the plan insofar as such documents and instruments are

consistent with the provisions of this title or title IV.

29 U.S.C. Sec. 1109, provides:

> (a) Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this title shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary. A fiduciary may also be removed for a violation of section 411 of this Act.
>
> (b) No fiduciary shall be liable with respect to a breach of fiduciary duty under this title if such breach was committed before he became a fiduciary or after he ceased to be a fiduciary.

STATEMENT OF THE CASE

The jurisdiction of the bankruptcy court was invoked under 28 U.S.C. 1334 and 157 (a) and

(b)(2)(A), (B), (N) and (O). The jurisdiction of the district court was invoked under 28 U.S.C. 158(a). The jurisdiction of the court of appeals was invoked under 28 U.S.C. 158(d).

Petitioners sued Philip Zinke and his wife for constructive trust arising from Zinke's misapplication of funds from Stonehenge and Harbison-Fischer in purchasing a personal residence for Zinke. Philip Zinke was an investment advisor and broker who was subsequently convicted of serious unrelated crimes.[1] Zinke solicited money from multiple investment clients over a period of years, for

---

[1] People v. Zinke, 147 A.D. 106, 541 N.Y.S.2d 986 (1st Dept. 1989, reversed as to criminal liability, 76 N.Y.2d 8, 556 N.Y.S.2d 11 (1990); U.S. v. Zinke, et al., 92 Cr. 899 (PNL), U.S. Dist. Ct. S.D.N.Y. 1991. In August, 1987, Zinke was convicted after a jury trial in New York State Court on two counts of grand larceny "for embezzling $1.05 million in mid-1984 from Stonehenge." People v. Zinke, 541 N.Y.S.2d 986. The conviction was affirmed by the Appellate Division, First Department, but reversed by the Court of Appeals on the technical ground that as a matter of law the general partner of a limited partnership cannot be charged with the crime of larceny from the limited partnership. People v. Zinke, 556 N.Y.S.2d 11 (1990). Although Zinke escaped criminal liability, Zinke admitted the $1.05 million has never been returned or repaid.

investments for the clients' ERISA qualified pension funds. Without the clients' knowledge or consent, he used several million dollars of the clients' money to purchase a personal residence and a commercial building, for his personal use.

Philip Zinke was the general partner of Stonehenge. Zinke was the investment manager of the H-F pension plan. H-F's pension plan was a limited partner in Stonehenge. Zinke was an ERISA fiduciary to Stonehenge. No evidence was presented to contradict the status of Zinke as a fiduciary to Stonehenge.

After his scheme was partially uncovered, the victimized investment clients, including Petitioners Stonehenge and H-F, sought to recover their money by seizing the personal residence.

Zinke's wife filed bankruptcy and obtained an order from the bankruptcy court with jurisdiction of her case allowing the residence to be sold free and clear of liens, but subject to the constructive trust claims of Petitioners. Internal

Revenue Service and the State of New York appeared in the bankruptcy court in support of the sale of the personal residence free and clear of liens. Zinke's wife asked the bankruptcy court to allow payment of IRS and the State of New York, pending resolution of the constructive trust claims. The bankruptcy court authorized payment of the tax claims, subject to the court's later determination that the constructive trust claims were valid and requiring the tax authorities to refund the tax payments.

Petitioners proved their money was used by Zinke on the personal purchases, but Zinke claimed he legally "borrowed" the money and any profit on the deals was his to keep (and to pay his personal taxes) even though Stonehenge remains unpaid.[2]

Zinke failed to disclose these transactions to anyone involved in Stonehenge (including H-F).

---

[2] Unless otherwise stated, references to the trial transcript are to August 5, 1991.

Stonehenge asserted Zinke embezzled the money, and breached his fiduciary obligations to Stonehenge. Zinke claims it was a loan he as the general partner for Stonehenge made to himself and that he had the right to "self deal."

Zinke pointed to written notes signed after the money was used by him as evidence of his "loan" from H-F. He admitted he never told H-F of his plan to use the money for his personal purchase because "it's not any of their business." One year after receiving the funds, Zinke represented in writing to the outside auditors for Petitioner H-F that the funds were invested as the client originally understood, and said nothing about his personal purchase.

The Bankruptcy Court found that Zinke's status as a common law and ERISA fiduciary to the victims over several years, did not prevent him from engaging in side deals with the Petitioners, even though he did not tell them he was not acting in a fiduciary role in the side deals with them.

The Bankruptcy Court held that the Petitioners had the burden of proof on the case and did not meet it. The Court also stated "if the burden was on the other side I could possibly rule the other way."

The Bankruptcy Court held that H-F was paid back on the personal residence "loan," and Stonehenge had no remedy against the Apartment sale proceeds even though the so-called loan repayment to H-F came from funds on which Stonehenge had a claim. In effect, the Bankruptcy Court held that Zinke's tax authorities had a higher priority claim than either of the Petitioners.

The District Court upheld the Bankruptcy Court's decision because the burden of proof was on Petitioners to do so on a basis of "clear and convincing evidence."

The statement at the oral argument to the bankruptcy counsel by counsel for Stonehenge that Stonehenge could not "trace its funds to the co-op, but only to H-F," was in error and not a waiver of

the evidence presented at the trial. Zinke admitted that Stonehenge funds were used to purchase the commercial building. Zinke asserted that H-F was paid out of the proceeds of the commercial building refinance. While Petitioners continue to except to the assertion by Zinke, even if Zinke's assertion is deemed true as found by the bankruptcy court, Zinke's testimony clearly traces Stonehenge funds to the personal residence transaction. In other words, the only way that H-F could have been repaid on the personal residence transaction was for Stonehenge's interest in the commercial building to have been substituted for H-F's interest in the personal residence. As a result, Zinke was robbing Peter to pay Paul.

Upon timely appeal to the United States Court of Appeals for the Second Circuit, the Second Circuit affirmed the lower court opinion, and specifically stated that the burden of proof was on the Petitioners to prove tracing and the elements of the constructive trust.

Each of the lower courts ignored the admission by Zinke that he was an ERISA fiduciary to the H-F pension plan and other pension plans that were limited partners of Stonehenge Insured Notes. Zinke also admitted that he was the general partner of Stonehenge, and that he used Stonehenge funds and H-F funds to purchase his personal residence. Zinke claimed that his use of H-F funds was permissible because the funds were loaned to him by H-F. The bankruptcy court held that the transaction between H-F and Zinke was a loan. Zinke claimed that he was not a fiduciary to H-F in connection with the loan despite his admitted fiduciary status to H-F's pension plan.

Each of the lower courts held that no tracing of assets from Stonehenge to the Zinke residence was proved by the Petitioners. No contention was ever made by any party to the case that Zinke communicated a termination of his fiduciary

relationship to Stonehenge, H-F, nor any other limited partner of Stonehenge.

REASONS FOR GRANTING THE PETITION

I. Fiduciary and Non-Fiduciary Obligations under ERISA

The opinions of the lower courts in this case eviscerate the public policy to protect ERISA beneficiaries and participants from fraud and self-dealing by ERISA fiduciaries. This case provided a strong test of the application of the fiduciary obligations of ERISA to a case in which the fiduciary admitted self-dealing with qualified plan assets.

In Mertens v. Hewitt Associates, 508 U.S. 113, 113 S. Ct. 2063, 124 L. Ed.2d 161 (1993), the Court stated that ERISA makes fiduciaries liable for breach of fiduciary duties, including avoidance of conflicts of interest, and self-dealing Mertens v. Hewitt Associates, 508 U.S. 113, 113 S.Ct. 2063, 124 L.Ed.2d 161, 167 (1993), and

> specifies the remedies available against them: the fiduciary is personally liable for damages. . . for restitution ('to restore to [the] plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary'), and for 'such other equitable and remedial as the court may deem appropriate,' including removal of the fiduciary. §502(a)(2), 29 U.S.C. §1132(a)(2).

Mertens, 124 L.Ed.2d 161, 167.

At the same time, the majority opinion in Mertens reserved for determination the issue of whether ERISA imposed liability for a non-fiduciary's participation (knowing or unknowing) in a fiduciary's breach of fiduciary duty. Mertens, 124 L.Ed.2d 161, 169.

As a result, this case presents an opportunity to determine whether a non-fiduciary is subject to equitable relief under ERISA, and further to delineate under ERISA the fine line between fiduciary obligations and the obligations of a non-fiduciary.

Petitioners firmly believe that Zinke was a fiduciary both to Stonehenge and its component limited partners, including H-F's pension plan, but also to H-F itself as the plan sponsor of H-F's pension plan.

Even if Zinke was determined to be a non-fiduciary with respect to the funds he acquired from H-F, Petitioners assert that he was liable as a party-in-interest and a non-fiduciary for knowing participation in a breach of his fiduciary duties with respect to Stonehenge funds.

II. The Decision of the Court of Appeals is Erroneous

Cases interpreting ERISA have uniformly held that the burden of proof is on a fiduciary to prove his conduct proper after a threshold showing of blatant fiduciary misconduct, such as self-dealing with plan assets. See Marshall v. Snyder, 572 F.2d 894 (2nd Cir. 1978), in which the court made it clear that the party representing plan beneficiaries who challenges a fiduciary's conduct in a

transaction in self-dealing does not have the burden of proving the unfairness of the transaction, and the burden of proof is on the fiduciary to the transaction where self-dealing is alleged. Also see Donovan v. Cunningham, 716 F.2d 1455, 1467-1468 (5th Cir. 1983), cert. denied, 467 U.S. 1251 (1983), Whitfield v. Lindemann, 853 F.2d 1298 (5th Cir. 1988). Also see Donovan v. Bierwirth, 754 F.2d 1049 (2nd Cir. 1985). In Leigh v. Engle, where fiduciaries benefitted from the improper use of plan assets, the court required the fiduciaries to meet the burden of tracing the profits which were attributable to their own investments and which were attributable to plan assets. Leigh v. Engle, 727 F.2d 113, 138 (7th Cir. 1984). Finally, the Second Circuit held in New York State Teamsters Council Health and Hospital Fund v. Estate of DePerno, when a plan showed fiduciary violations, even if no losses due to those violations were shown, the burden shifted to the defendant fiduciaries who had allegedly breached their duty,

to demonstrate that the expenditures were reasonably necessary and that the value received at least equalled the sums paid." New York State Teamsters Council Health and Hospital Fund v. Estate of DePerno, 18 F.3d 179 (2nd Cir. 1994).

III. The Court of Appeals' Interpretation of the Burden of Proof under ERISA

The Court of Appeals' interpretation of the burden of proof under ERISA conflicts with other circuits' interpretations, and other cases within the Second Circuit. The cases cited above all conflict with the Court of Appeals' opinion in this case. The Petitioners request for in banc consideration was denied below.

The interaction of the Mertens opinion with Lowen v. Tower Asset Management, Inc., 829 F.2d 1209 (2nd Cir. 1987), may be a cause for interpretative concern by the Court of Appeals for the Second Circuit. Therefore, this case presents an opportunity for the Court to resolve the differences between the circuits in light of the

Mertens case, and to further define the principles underlying Mertens and the unanswered issues presented thereby.

IV. The Questions Presented are Important

ERISA was passed by Congress out of concern that pension funds "were being corruptly or ineptly mismanaged and that American workers were losing their financial security in retirement as a result." Mertens, 124 L.Ed2d 161, 175, dissenting opinion of Justice White.

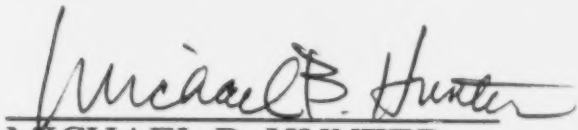
Congress enacted ERISA "to protect . . . the interests of participants in employee benefit plans and their beneficiaries, by requiring the disclosure and reporting to participants and beneficiaries of financial and other information with respect [to the plan], by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies, and ready access to the Federal Courts." 29 U.S.C. §1001(b). Mertens, 124 L.Ed.2d 161, 175.

Fiduciary obligations, or the denial of such obligations, are critical components of the economy and citizens' well-being. As the citizenry ages and becomes focused on retirement funding, establishing more definite standards for conduct of fiduciaries or non-fiduciaries with respect to retirement funds is a critical need. If liability should attach, then establishment of the rules for such conduct will enhance that aspect. If ERISA's broad provisions should not be expanded to non-fiduciaries, a clear indication of that determination will avoid clogging the courts with unwarranted claims against non-fiduciaries.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,



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August, 1995

Supreme Court, U.S.
FILED

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In The

SUPREME COURT
OF THE UNITED STATES
October Term, 1995

STONEHENGE INSURED NOTES-I LIMITED PARTNERSHIP; AND HARBISON-FISCHER MFG. CO., INC., *Petitioners*,

v.

UNITED STATES DEPARTMENT OF THE TREASURY, STATE OF NEW YORK, and PHILIP ZINKE, *Respondents*.

Appendix to Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

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APPENDIX

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UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 19th day of May one thousand nine hundred and ninety-five.

In Re: JUDITH A. ZINKE
Debtor

JUDITH A. ZINKE, also known as Judith Zorn,
Plaintiff-Appellee,

v.

STONEHENGE INSURED NOTES - I LIMITED PARTNERSHIP ("SIN-I"); and HARBISON-FISCHER MFG. CO., INC.,
Appellants,

-v.- DOCKET NOS. 94-5031(L)
UNITED STATES DEPARTMENT 94-5033
OF THE TREASURY,
STATE OF NEW YORK and PHILIP ZINKE,
Defendants-Appellees,

GOODMAN PLUMBING AND HEATING CORP.; ROBERT ABRUSSO; STRAZZEN & SON; ENVIRONMENTAL CONTROL BOARD; V.A. PARADISE, as Trustee for Schiavone Construction Company Pension Trust; and JOHN AND JANE DOES, being individuals, partnerships, corporation or other entities whose real names are unknown, who may have an interest in the property to be sold.
Defendants.

A petition for rehearing containing a suggestion that the action be reheard in banc having been filed herein by Appellants STONEHENGE INSURED NOTES-I LIMITED PARTNERSHIPS ("SIN-I") and HARBISON-FISCHER MFG. CO., INC.,

Upon consideration by the panel that decided the appeal, it is

ordered that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges of the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

FOR THE COURT,
GEORGE LANGE III, Clerk
By:

_____

Carolyn Clark Campbell
Chief Deputy Clerk

EDNY
93-CV-718
GLASSER

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 10 day of January one thousand nine hundred and ninety-five.

Present:

Honorable Ellsworth A. Van Graafeiland,
Honorable John M. Walker, Jr.,
Honorable José A. Cabranes,
Circuit Judges.

In Re: JUDITH A. ZINKE
Debtor

JUDITH A. ZINKE, also known as Judith Zorn,
Plaintiff-Appellee,

v.

STONEHENGE INSURED NOTES - I LIMITED PARTNERSHIP ("SIN-I"); and HARBISON-FISCHER MFG. CO., INC.,
Appellants,

v.

ORDER
#S 94-5031,5033

UNITED STATES DEPARTMENT OF THE TREASURY, STATE OF NEW YORK and PHILIP ZINKE,

Defendants-Appellees,

GOODMAN PLUMBING AND HEATING CORP.; ROBERT ABRUSSO; STRAZZEN & SON; ENVIRONMENTAL CONTROL BOARD; V.A. PARADISE, as Trustee for Schiavone Construction Company Pension Trust; and JOHN AND JANE DOES, being individuals, partnerships, corporation or other entities whose real names are unknown, who may have an interest in the property to be sold,

Defendants.

Appeal from a judgment entered in the United States District Court for the Eastern District of New York (I. Leo Glasser, J.).

This cause came to be heard on the transcript of record and was argued.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed.

SIN-I and Harbison Fischer appeal from a judgment of the district court (Glasser, J.), entered February 24, 1994, affirming orders of the bankruptcy court (Hall, B.J.) which denied both appellants' request that a constructive trust in their favor be imposed on the proceeds of the sale of the Zinkes' Fifth Avenue apartment, and appellants' motion for new trial.

Philip Zinke was an investment manager for Harbison-Fischer's retirement plan. On May 31, 1983, Zinke asked Harbison-Fischer, the corporation, to wire $1.5 million of its corporate funds (not its pension funds) to Citibank in New York. After receiving the money, Zinke used $810,000 of that amount to purchase a Fifth Avenue apartment.

Zinke was also the general partner of SIN-I. In April and July 1984, Zinke wrote two checks totalling $1.05 million on SIN-I's bank account to help purchase a building on 54th Street in Manhattan (the "Famolare building").

On November 3, 1987, Judith Zinke, Philip's wife and the debtor, sought the bankruptcy court's approval of the sale of the Fifth Avenue apartment free and clear of liens and other encumbrances, with the proceeds to satisfy federal and state tax liens. Harbison-Fischer and SIN-I both sought to have the bankruptcy court impose constructive trusts against the proceeds in their favor. The bankruptcy court denied their claims.

Appellants make several arguments on appeal. They argue first that the district court and bankruptcy court erred in finding that Philip Zinke was not an ERISA or common law fiduciary with respect to Harbison-Fischer. If Zinke was a fiduciary to Harbison-Fischer, appellants' claim to a constructive trust would be considerably stronger. Because the bankruptcy court found that the $1.5 million transfer to Zinke was a loan, it concluded that the relationship between Harbison-Fischer and Zinke was an ordinary one of creditor/debtor. The district court agreed with the bankruptcy court's finding, noting that Zinke's role as an investment manager of the Harbison-Fischer pension plan was of no consequence since the $1.5 million transfer was

made by the Harbison-Fischer corporation and no evidence suggested Zinke had made any investments for the corporation. We agree with the district court that it was not clearly error for the bankruptcy court to find that the $1.5 million transfer was a loan because the only documentary evidence - two notes signed by the counsel for Harbison-Fischer - indicate that the corporation treated the $1.5 million transfer as a loan. Relying on that finding, see United States v. McCombs, 30 F.3d 310, 316-17 (2d Cir. 1994) (stating that findings of fact shall not be set aside unless clearly erroneous), we conclude, as did the bankruptcy court and district court, that Zinke was not a fiduciary to Harbison-Fischer. See In re Koreag, Controle et Revision S.A., 961 F.2d 341, 353 (2d Cir. 1992) ("Purely commercial transactions do not give rise to a fiduciary relationship.").

Appellants argue next that the district court erred in proceeding to consider whether factors other than the existence of a fiduciary relationship would warrant imposing a constructive trust in this case (viz., express or implied promise, reliance, unjust enrichment, see id. at 352). They argue that the district court should have remanded the case for further fact finding once it found that the bankruptcy court erred in considering only one factor in the constructive trust analysis. The additional "findings" that the district court made, however, were essentially legal conclusions which followed logically from findings of fact made by the bankruptcy court. For example, the district court's conclusion that Zinke had not been unjustly enriched was based in large part on the bankruptcy court's finding that the $1.5 million loan was "repaid in full, inclusive of interest, out of the proceeds of a refinancing with respect to a certain property owned by Philip Zinke." App. 572-73. This finding by the bankruptcy court was not clearly

erroneous. Charles Fischer, president and chairman of Harbison-Fischer, admitted that Harbison-Fischer received approximately $10 million when Zinke refinanced the mortgage on the Famolare building in January 1985 even though the balance due on the mortgage was only $8.1 million. While testifying that the additional $1.9 million Harbison-Fischer received (which approximated the amount Zinke owed on the asserted loan, including interest) did not include the $1.5 million Harbison-Fischer had transferred to Zinke, Fischer did not provide a convincing alternative explanation for the additional amount received.

Because the bankruptcy court's finding that the $1.5 million transfer was a loan that Zinke repaid with interest was not clearly erroneous, the district court did not err in concluding that appellants failed to prove either a fiduciary relationship or unjust enrichment. In light of this failure of proof, we conclude that neither court abused its discretion in declining to impose a constructive trust in favor of Harbison-Fischer on the proceeds of the sale of the Fifth Avenue apartment.

SIN-I's constructive trust claim cannot survive the failure of Harbison-Fischer's claim. SIN-I's claim is based on $1.05 million that Zinke took from SIN-I to help purchase the Famolare building. As this court has stated before, "[i]t is hornbook law that before a constructive trust may be imposed, a claimant to a wrongdoer's property must trace his own property into a product in the hands of the wrongdoer." United States v. Benitez, 779 F.2d 135, 140 (2d Cir. 1985). At trial before the bankruptcy court, counsel for SIN-I conceded that the funds SIN-I lost could not be traced to the Fifth Avenue apartment and that its claim for a constructive trust was therefore dependent on Harbison-Fischer's claim:

> SIN-I . . . cannot trace its funds to the co-op but only to Harbison-Fischer. . . .
>
> . . . .
>
> . . . . SIN-I, therefore, will ask the Court in the exercise of its equitable powers to impose a constructive trust in favor of Harbison-Fischer on all the proceeds of sale of the co-op and then to further impose a constructive trust in favor of SIN-I against the Harbison-Fischer constructive trust proceeds . . .
>
> .

App. 538-39 (emphasis added). Because SIN-I cannot trace its funds to the apartment proceeds and because Harbison-Fischer failed to secure a constructive trust in its favor, SIN-I's claim fails as well.

Appellants also argue that the district court and bankruptcy court erred in denying their motion for new trial pursuant to Rule 59 of the Federal Rules of Civil Procedure to permit the presentation of newly discovered evidence and to redress alleged misconduct by the United States. We disagree. First, "[s]uch decisions are reversible only if the trial judge clearly abused his discretion." Philip v. Mayer, Rothkopf Industries, Inc., 635 F.2d 1056, 1063 (2d Cir. 1980). Second, in order to warrant a new trial, "newly discovered evidence" must be evidence that would likely have led to a different outcome at trial and that could not have been discovered in the exercise of due diligence before trial. Id. Here, evidence of Zinke's prior convictions and past cooperation with the government could have been discovered before trial and, in any event, would not have altered the outcome of the trial before Bankruptcy Judge Hall. See Decision and Order On Motion For New Trial, Clarification of Ruling, And/Or Alternation Or Amendment Of Judgment, at 11, App. 606. Third, in light of the affidavit by Patricia Henry, trial counsel for the United

States, the courts reasonably found that the government did not conceal from appellants its knowledge of Zinke's whereabouts before the August 1991 bankruptcy court trial.

We have reviewed appellants other claims and deem them to be without merit. Accordingly, the judgment of the district court is AFFIRMED.

Hon. Ellsworth A. Van Graafeiland, U.S.C.J.

Hon. John M. Walker, Jr., U.S.C.J.

Hon. José A. Cabranes, U.S.C.J.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

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In re
JUDITH A. ZINKE, a/k/a JUDITH ZINKE, JUDITH ZORN,

Debtor.

----------x

JUDITH A. ZINKE,

Plaintiff

-against-

JUDGMENT
93-CV-0718 (ILG)

UNITED STATES DEPARTMENT OF THE TREASURY; NEW YORK STATE TAX COMMISSION; CITY OF NEW YORK DEPARTMENT OF FINANCE; SHERMAN, CITRON, KARASIK; DEJET SYSTEMS; DENWELL CONTRACTORS, INC.; GOODMAN PLUMBING & HEATING CORP.; ROBERT ABRUSSO; STRAZZEN & SON; ENVIRONMENTAL CONTROL BOARD; V.A. PARADISE; PHILIP ZINKE, JOHN DOES AND JANE DOES, et al..,

Defendants.

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A memorandum and order of Honorable I. Leo Glasser, United States District Judge, having been filed on February 14, 1994, affirming in their entirety the September

25, 1991 and December 22, 1992 orders of the bankruptcy court, it is

ORDERED and ADJUDGED that the September 25, 1991 and December 22, 1992 orders of the bankruptcy court are affirmed in their entirety.

Dated: Brooklyn, New York
February 24, 1994

Robert C. Heinemann
Clerk of Court

By: _____
James Giokas
Chief Deputy Clerk

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

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In re
JUDITH A. ZINKE,
a/k/a JUDITH ZINKE,
JUDITH ZORN,

CASE NO. 887-71461-20
IN BANKRUPTCY

Debtor.
----------x

JUDITH A. ZINKE,

Plaintiff

-against-

MEMORANDUM AND ORDER

UNITED STATES DEPARTMENT OF THE TREASURY; NEW YORK STATE TAX COMMISSION; CITY OF NEW YORK DEPARTMENT OF FINANCE; SHERMAN, CITRON, KARASIK; DEJET SYSTEMS; DENWELL CONTRACTORS, INC.; GOODMAN PLUMBING & HEATING CORP.; ROBERT ABRUSSO; STRAZZEN & SON; ENVIRONMENTAL CONTROL BOARD; V.A. PARADISE; PHILIP ZINKE, JOHN DOES AND JANE DOES, et al..,

Defendants.
----------x

GLASSER, UNITED STATES DISTRICT JUDGE:

FACTS

This is an appeal from orders of the United States Bankruptcy Court for the Eastern District of New York, entered on September 25, 1991 and December 22, 1992, by Judge Robert John Hall. This case has had a long history before both the bankruptcy court and this court; for purposes of this appeal, the relevant facts are as follows.

Background

On September 29, 1987, Judith Zinke (the "debtor") filed a voluntary petition under Chapter 11 of the Bankruptcy Code, 11 U.S.C. §§ 101 et seq. Shortly thereafter, on November 3, 1987, the debtor commenced these adversary proceedings pursuant to 11 U.S.C. § 363(h), seeking to sell the shares of a cooperative apartment located at 1010 Fifth Avenue, New York, New York (the "property") free and clear of all encumbrances. The debtor sought to use the proceeds of the sale to satisfy tax liens by the United States Department of Treasury and the New York State Department of Taxation and Finance (collectively, the "taxing authorities"); the debtor also sought a declaratory determination that no other party had a claim to the property.

The bankruptcy court entered an order on December 2, 1987, authorizing the sale of the property free and clear of all liens, encumbrances and claims. The bankruptcy court also authorized the debtor to satisfy the tax liens without prejudice to the rights of competing claimants to the proceeds, and further ordered that "the taxing authorities shall continue to remain subject to the jurisdiction of this Court to determine any and all claims raised in the adversary proceedings or with regard to any

claim for the recovery of funds paid to the taxing authorities pursuant to the Order." Finally, the court directed that the balance of the proceeds of the sale be held in an escrow account by the debtor's attorney. (152).[1] This court affirmed Judge Hall's decision in a memorandum and order dated February 28, 1989.

Claims against the proceeds from the sale of the property subsequently were asserted by two parties: Harbison-Fischer Manufacturing Company ("H-F"), a corporation incorporated under the laws of Texas and having its principal place of business in Texas; and Stonehenge Insured Notes I, Ltd. ("SIN-I"), a limited partnership organized under the laws of Delaware.[2] Specifically, both H-F and SIN-I alleged that a constructive trust should be impressed in their favor upon the proceeds from the sale of the property.[3] The bankruptcy court conducted a trial on August 5 and 6, 1991 to determine the

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[1]Catations to the Joint Record of SIN-I and Harbison-Fischer Mfg. Co., Inc. will be designated solely by the appropriate page numbers in the record. Citations to the Amended Counter Designation of the Record and Statement of Issues on Appeal submitted by the United States will be designated "Gov't Item at __". Citations to the Transcript from oral argument before this court on January 26, 1994 will be designated "Tr. __."

[2]SIN-I currently is the subject of Chapter 11 bankruptcy proceedings in the United States Bankruptcy Court for the Northern District of Texas. (193).

[3]By Memorandum and Order dated May 31, 1991, this court ruled, inter alia, that the bankruptcy court did not abuse its discretion in holding (in an order entered February 26, 1991) that the paper submitted by H-F was sufficient to be treated as an objection or answer, and in permitting H-F to amend its answer to assert the constructive trust claim.

claims against the property. Ruling from the bench, Judge Hall held that H-F and SIN-I had not carried their burden of establishing constructive trust claims to the property. The bankruptcy court expanded upon this holding in findings of act and conclusions of law dated September 25, 1991, and in a decision and order dated December 22, 1992.

Trial

Three witnesses testified at trial: The first witness was Philip Zinke ("Zinke"), the debtor's husband, who was the manager of H-F's Retirement Plan (the "Plan"), but who apparently had no employment or other affiliation with H-F, an entity separate and distinct from the Plan; Zinke also was the general partner of SIN-I. The other witnesses were Charles Fischer, the President and Chairman of H-F, and Roy Bracken, the Chief Financial Officer of H-F. Although many of the facts are contested by the parties, the following events are not disputed.

On May 31, 1983, H-F wired $1.5 million of its corporate funds to Citibank in New York, which was deposited in an account in the name of Park Place Associates, an association of which Zinke was President. The following day, $810,000 was transferred from the Park Place Associates account to an account bearing the name Philip Paige, Staunton and Greer, Ltd. ("Philip Paige"), a corporation of which Zinke was President. A cashier's check in the amount of $810,000 then was issued from the Philip Paige account and delivered to the seller of the property. (See 1200-18). Various documents evidence the purchase of the property by Philip and Judith Zinke and show that the closing occurred on June 2, 1983. (1219-42).

In April 1984, Zinke wrote a check in the amount of $250,000 on SIN-I's account at Benham Capital Management Group payable to Messrs. Joseph and Leo Famolare. On July 5, 1984, Zinke wrote another check for $800,000 on the same account payable to the same individuals.[4] These funds were used, in part, to purchase a building at 4 East 54th Street in Manhattan (the "Famolare Building"). Zinke has conceded that he has not returned to SIN-I the $1.05 million drawn from its accounts. (495).[5]

In August 1984, H-F -- the corporation, not the Plan -- invested $7.9 million through Zinke in the purchase of the Famolare Building; this investment was secured by a mortgage on the building and contained an "equity kicker" in the building. Zinke refinanced the Famolare Building in January 1985, at which time H-F was paid approximately $10 million.[6]

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[4]Zinke testified that he executed demand notes reflecting the transactions which designated him as borrower, the notes were not secured by any collateral and have not been produced in these proceedings. (471-72).

[5]Zinke testified, however, that he sought to settle the notes in 1987 by paying the principal, the interest and the accumulated legal fees; this offer was rejected. (516-17). In August 1987, Zinke was convicted of two counts of grand larceny in the second degree after a jury trial in New York State Supreme Court "for embezzling (sic) $1.05 million in mid-1984 from SIN-I." The New York Court of Appeals ultimately reversed the conviction because "in New York, partners cannot be charged with larceny for misappropriating firm assets." People v. Zinke, 76 N.Y.2d 8, 13, 556 N.Y.S.2d 11, 14 (1990).

[6]It bears noting that at oral argument, counsel was extremely vague with regard to who took title to the Famolare Building; to whom it ultimately was sold; and for how much it was sold. E.g.,

Although the occurrence of the above-described events is undisputed, as indicated by the conflicting testimony of the witnesses at trial, many of the facts surrounding these events are contested by the parties.

A. Testimony of Philip Zinke

Zinke testified that he was the manager of the Plan in May 1983, and had been an investment advisor for the Plan since approximately 1974. He recollected that approximately six months prior to May 1983, he had proposed to Charles Fischer the idea of investing in a condominium parking garage in New York City, and that he outlined the investment concept in writing.[7] (435, 450; 1260-62). In addition, Zinke's attorney prepared a joint venture agreement in anticipation of finding property that would be satisfactory to Fischer; while this proposal was sent to H-F, it never was signed. (460-61; 1272-86). Zinke testified that he told Fischer that he needed to have ready access to funds in the event that property became available; Zinke alleges that in response, Fischer indicated that

> in order to facilitate the mutual objective of going ahead, that [Fischer] was prepared to send the funds to me to use as I saw fit as a personal loan and if then I wanted to commit

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Tr. 40, 48-49.

[7]The written proposal, titled "'Park Place' Condominium Park Facility Proposal," described the operation as a "joint venture" between H-F and Philip Paige "to develop, market and manage condominium parking places in a series of locations in metropolitan areas lacking adequate parking facilities." The proposal anticipated that Philip Paige would organize Park Place Associates to be jointly owned by Philip Paige and H-F. (1260).

> on the basis of my own feelings, at my own risk, that I could and then I would be able to come to him and say look, here's what I've gone ahead with. Here's the specifics. If he then liked the deal, then we would renegotiate and go back to the original sense of the going (sic) venture but the idea was always to go forward but that funds would be made available to me as a personal loan to go forward on anything I wanted to and then to come to him and be subject to his consideration.

(436-37) (emphasis added).

On May 31, 1983, H-F transferred $1.5 million to Zinke, which transaction was evidenced by a notes prepared by H-F's counsel, dated May 31, 1983, int he principal amount of $1.5 million.[8] (437-38; 1098). Zinke testified that in the fall of 1984, he was given a second note prepared by H-F, dated October 1, 1984, in the principal amount of $1,753,868.44; this note reflected the interest that had accrued on the principal at that time, and was secured by an interest in the Famolare Building.[9] (440, 1118-23).

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[8]The makers of the note were identified as Zinke, individually, and Philip Paige, a New York corporation. Zinke testified that he believed the note had been signed in Fort Worth, Texas on or about May 31. (528-30). H-F alleges that the note in fact was not signed until October 1984, at which time it was backdated to reflect the May transaction.

[9]Zinke recollected that the second note also was signed in Fort Worth, Texas. (530).

By letter dated December 3, 1984, Bracken notified Zinke that his "personal note" to H-F dated October 1, 1984, adjusted for accrued interest through November 30, 1984, reflected a current value of $1,790,452.24. (1124). The letter also noted that interest had accrued on the $7.9 million of mortgage money H-F had invested in the Famolare Building, resulting in a total balance of $8,081,075.65. (1124).

On cross-examination, a letter dated June 6, 1984 from Zinke to a Mr. Stephens at Arthur Young & Company was introduced into evidence. The letter stated in relevant part:

> [W]e herein confirm that Harbison-Fischer Manufacturing Company has invested $1.5 million in a joint venture controlled by our firm named Park Place Associates. The partnership will be marketing New York City's first condominium garage project on or about 1 September 1984.

(462; 1287). Zinke testified that he wrote the letter in accordance with Fischer's wishes, and that for accounting purposes, he was asked to characterize the proposed transaction as a joint venture. (554, 557).

Zinke testified that when the Famolare Building was refinanced in January 1985, he paid off both the $1.5 million and the mortgage obligation with the $10 million transfer to H-F; this payment is evidenced by a certified check payable to H-F in the amount of $10 million. (444-45; 1125).

B. Testimony of Charles Fischer

Fischer testified that H-F "propose[d] (sic) trust and confidence into Philip Zinke in making . . . investments." (562). He indicated that over a period of weeks prior to May 31, 1983, Zinke mentioned the idea of a condominium parking garage several times. (563-64). Zinke provided him with a map of New York showing three potential sites for the garage in Brooklyn, together with the parking garage proposal. (565-66). Fischer testified that Zinke represented that he was negotiating with different people and "he needed to have good collective (sic) cash up in New York where he could act very swiftly, if necessary, and also show that he had substantial funds, he could pull off this type of purchase." (566). According to Fischer, H-F sent the $1.5 million on May 31 to the Park Place Associates account because it "wanted to allow Mr. Zinke to show substance that he could make a deal for real estate when the moment arrived which we anticipated to be in the very near future." (567). Subsequent to the transfer of funds, Fischer talked with Zinke every few weeks and Zinke informed him that he was looking at potential sites in Manhattan and Brooklyn and "hoped to clear a deal for that in the near future." (568). Fischer alleged that Zinke also told him on more than one occasion that the money was in an interest-bearing account in Citibank. (568).

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[10]At oral argument, counsel for SIN-I conceded that although Zinke had made investments on behalf of the Plan, the evidence showed that Zinke previously had invested no money on behalf of H-F, the corporation. (Tr. 24). Moreover, counsel conceded that the investment in the condominium parking garage would not have been an appropriate investment for the Plan. (Tr. 23).

With respect to the notes, Fischer testified that prior to October 2, 1984, H-F had no evidence of the transfer of $1.5 million to Zinke.[11] (569). Fischer contended that Zinke executed both notes in Texas on October 2, but conceded that the notes were "handled" by H-F's financial officer and counsel. (570). Fischer denied that Zinke had requested a personal loan from H-F or that he ever had asked to use a portion of the $1.5 million for personal reasons. (570-71). He testified that Zinke never told him that he put $810,000 of the $1.5 million into the property; that Zinke never told him the $1.5 million was in any place other than an interest bearing account; and that Zinke never repaid or returned the $1.5 million to H-F. (571-72). Fischer indicated that he first learned that $810,000 of the $1.5 million was used to purchase the property when Citibank's records were subpoenaed in 1986.[12] (575).

Fischer testified that at the time of the refinancing of the Famolare Building in January 1985, H-F received approximately $10 million. (576). Fischer conceded that $8.1 million of this amount represented H-F's investment in the building; that given the ultimate sale price of $11.5 million, H-F's 50% "equity kicker" would be somewhere

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[11]On cross-examination, in response to the question "Now, you're telling us that you advanced a million and a half and you didn't even take back a note or any kind of letter understanding as to what the agreement was between the parties; is that what you're telling the Court?" Fischer replied "That's right, yes." (588).

[12]Fischer also denied having a conversation with Zinke about the letter Zinke sent to Arthur Young on June 6, 1984. (569).

between $500,000 and &750,000;[13] that at the time of closing, $250,000 was escrowed in anticipation of the equity kicker; and that the difference between the $10 million and the $81. million therefore could not be attributed to the equity kicker. (577-79). In addition, Fischer acknowledged that he never made a demand for the balance of the $1.8 million due on the original $1.5 million note; that notwithstanding H-F's security interest in the Famolare Building, he did not insist that the $1.8 million be paid out at the closing; and that he never commenced a lawsuit to recover the funds or asserted a counter claim for the funds in a litigation over the $250,000 between H-F and Zinke pending in Texas. (588-588A).

C. Testimony of Roy Bracken

The final witness to testify at trial was Roy Bracken, who became the Chief Financial Officer of H-F on August 1, 1984. (605). Bracken recollected that when he commenced employment, he was concerned to discover that the parking garage venture had not been consummated and that there was no documentation with respect to the $1.5 million transfer or the payment of interest on that transfer. (606). In addition, he indicated that sometime before October 1984, Zinke had advised Fischer "that the parking condominium project was disbanded or was abandoned. That there was no longer any intention to proceed with that investment." (623). Bracken accordingly contacted counsel for H-F, who ultimately drafted the two notes, one which was backdated to May 31, 1983. (607-08; 623). However,

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[13]Alternatively, if the Famolare Building was sold to a party other than the parties negotiating at the time with Zinke, H-F would be entitled only to a 20% "equity kicker," bringing its share to between $200,000 and $300,000. (579-80).

Bracken emphasized that H-F always had considered the $1.5 million an investment; "[i]t was an investment in a limited parking garage which later took the form of the note but again, our initial intent was clearly an investment." (613).[14]

Regarding H-F's investment in the Famolare Building, Bracken testified that in January 1985, H-F assigned its mortgage and all its rights in the building to the Indonesian Bank for $10 million, and that return of the $1.5 million transfer was not contemplated during the negotiations for the assignment. (611-12; 634-35). Bracken testified that he was not concerned about getting paid the $1.5 million out of the proceeds of the refinancing (636), and that he never sent a demand letter to Zinke or commenced a lawsuit to recover the funds. (637). He testified to his understanding that H-F received almost $2 million above the approximately $8 million it was owed under the mortgage because it gave up its 50% equity kicker to the Indonesian Bank; however, Bracken then conceded that the refinancing agreement specifically provided that H-F would retain its equity kicker. (648).

The Rulings of the Bankruptcy Court

At the conclusion of trial on August 6, 1991, Judge Hall ruled from the bench. With respect to the $1.5 million transfer, Judge Hall found significant the absence of documentation concerning the transfer; Zinke's testimony

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[14]With respect to Zinke's June 6, 1984 letter to Arthur Young, Bracken opined that in the absence of documentation reflecting the $1.5 million transfer, Arthur Young would have requested the letter as independent verification of the investment from someone other than the management of the company.

that it was an unrestricted loan; the absence of signed documents reflecting a joint venture; and Zinke's testimony that he was entitled to take the money and invest it in the property. (738). Based on this evidence, Judge Hall held that the notes clearly indicated that the money was loaned to Zinke and Philip Page without restriction, evidencing a debtor/creditor relationship. (738).

Judge Hall ruled that H-F had failed to meet its burden of establishing a confidential relationship; he likened the relationship between Zinke and Fischer to that between a stockbroker and an investor. (738-39). He further noted that after the refinancing in January 1985, there was "no evidence that there was any debt still owed by Mr. Zinke to Harbison-Fischer until notice was sent out of the proposed sale and compromise, etc." (739). He therefore concluded that H-F was repaid the $1.5 million, and that H-F's failure to meet its burden of proof also defeated the claim of SIN-I.[15] (740).

Judge Hall's ruling was supplemented by findings of fact and conclusions of law dated September 25, 1991. Judge Hall's findings of fact were as follows:

1. The $1.5 million advanced by H-F was an interest bering loan, evidenced by the two "clear and unambiguous" promissory notes, and no restriction was placed on Zinke's use of the proceeds. (802).

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[15]Judge Hall remarked that "if the burden was on the other side I could possibly rule the other way but I feel that Harbison-Fischer has not met the burden and that sort of knocks them out and knocks SIN-I out." (740).

2. The $1.5 million obligation was repaid in full, including interest, out of the proceeds of the refinancing of the Famolare Building; H-F received $10 million from the refinancing, of which approximately $8.2 million related to the underlying mortgage held by H-F and $1.8 million related to the satisfaction of the notes. (802-03).

3. The documents prepared by H-F's counsel treated the transaction as a personal loan to Zinke, and the notes contradicted the "investment theory" urged by H-F. (806).

4. H-F's inaction until the notice of sale confirmed the nature of the transaction as a loan. (806).

5. H-F had the burden of proof, "and ha[d] failed to establish by any standard, a fiduciary or confidential relationship or that the transaction was an investment." (806).

6. With respect to Fischer's credibility, Judge Hall found that "although Mr. Fischer was trying to be direct and forthright, he was unable to justify or substantiate many of his own impressions and conclusions. Mr. Fischer appeared to the Court to be a man who relied heavily upon his own instincts and upon the other officers at Harbison-Fischer, rather than on any definite representations made by Mr. Zinke. Much of Mr. Fischer's testimony was vague." (806).

7. With respect to Zinke's credibility, Judge Hall found that the loan documents supported Zinke's testimony and that "the Court did not hear anything or see anything which would demonstrate that Mr. Zinke's testimony was not credible." (806).

Based on these findings of fact, Judge Hall's conclusions of law were as follows:

1. "It is well-settled that ordinary contractual relationships do not rise to the level of a fiduciary duty. To impress a constructive trust, there must be at least a wrongdoing greater than the non-payment of a debt . . . . In the present case, the facts indicate a loan transaction, which, in fact, was repaid. . . . Consequently, no constructive trust claim can be made out." (803).

2. Because the two notes evidencing the $1.5 million transfer were prepared by H-F's counsel and were clear and unambiguous on their face, any evidence H-F or SIN-I sought to interpose to contradict the terms of the notes was barred under the parol evidence rule. (803-04).

3. Because H-F's claim failed, SIN-I's claim was precluded "since its claim is based upon a subrogation to the Harbison-Fischer position." (804). Moreover, SIN-I's claim failed because no evidence was submitted to establish that Zinke improperly converted any of SIN-I's funds. (804).

The Motion for a New Trial

H-F and SIN-I subsequently moved the bankruptcy court for a new trial, for clarification of its ruling and/or for alteration or amendment of its judgment. Their motion was based primarily on the "new" evidence that Zinke had been convicted in the United States District Court for the Southern District of New York for criminal violations of the Internal Revenue Code and sentenced to six months of imprisonment. Because Zinke had cooperated with the United States in connection with certain unrelated criminal

matters, H-F and SIN-I inferred that the United States Attorney for the Eastern District of New York had knowledge of his whereabouts and had refused to disclose this information to them. H-F and SIN-I asserted that the refusal of the United States to disclose Zinke's whereabouts resulted in a "miscarriage of justice" necessitating a new trial. In the alternative, they argued that the bankruptcy court erred in allowing Zinke to testify at trial and that the record should be opened to allow evidence of the above-described facts.

After conducting a hearing on the motion on January 8, 1992, the bankruptcy court issued a decision and order dated December 22, 1992. Judge Hall held that Zinke's cooperation in 1990 with the United States did not lead to the conclusion that the United States could ascertain his whereabouts at the time of the trial on August 5 and 6, 1991, or that Zinke had cooperated with the United States in this case. (1087). The United States therefore did not have an "unfair advantage" and no miscarriage of justice occurred. (1987-88).

The court also found that "[t]he Movants' contentions that Mr. Zinke's testimony at the [t]rial was contrary to their information gathered in preparation therefore, and that as a result they were not prepared to examine Mr. Zinke, is devoid of substantive basis." (1088). The court based its conclusion primarily on the following factors: that H-F and SIN-I had failed to specify what testimony was contradictory; that they did not establish that their inability to depose Zinke was due to any act or omission by counsel for the United States; and that they failed to object to Zinke's testimony on direct examination and in fact conducted their own lengthy cross-examination of Zinke. (1088-91).

Judge Hall also rejected the argument that Zinke's conviction in the Southern District of New York and his cooperation with the government in that action constituted newly discovered evidence requiring a new trial. (1091). Specifically, Judge Hall found that the evidence -- which would have been introduced to impeach Zinke's credibility -- would not have changed the result; that "neither impeaching nor corroborative evidence constitutes 'newly discovered evidence' that forms a basis for the granting of a new trial"; and that with due diligence, H-F and SIN-I could have discovered the evidence before trial. (1091-92).[16]

H-F and SIN-I thereafter appealed Judge Hall's September 25 and December 22 orders to this court. The taxing authorities have asked this court to affirm the rulings of the bankruptcy court.[17] For the reasons set forth

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[16]With respect to that portion of the motion seeking clarification of the September 25 order, Judge Hall held that his decision was final appealable order that satisfied Bankruptcy Rule 9021. (1093). With respect to that portion of the motion seeking alternation or amendment of the decision to limit the relief to dismissal or denial of the constructive trust claim only, Judge Hall noted that because the constructive trust claim was the only issue pending before the court, amendment or alteration was unwarranted. (1094).

[17]While the New York State Department of Taxation and Finance has not submitted papers in opposition to the appeal, their counsel David Cook indicated in a telephone conversation with Chambers that the attorney general was adopting the position articulated by the United States in her brief, in addition to maintaining an Eleventh Amendment defense. The debtor has been dismissed as a party to these proceedings pursuant to an amended plan of reorganization dated June 24, 1993. See Exhibits annexed to Brief of Appellee United States of America on Appeal ("Gov't Br.").

below, the bankruptcy court's orders are hereby affirmed in their entirety.

DISCUSSION

Standard of Review

In its December 22 order, the bankruptcy court held that "[t]his is a core proceeding pursuant to section 157(b)(2)(A), (B), (N), and (O) of title 28." For the first time in these proceedings, H-F argues that "the issue of whether the cooperative apartment was property within the bankruptcy estate of Judith Zinke is a non-core proceeding," and that this court therefore should engage in a de novo review of the bankruptcy court's orders.

The bankruptcy court correctly found that the determination of whether a constructive trust should be imposed on the proceeds from the sale of the property is a core proceeding. Section 157(b)(2) of title 28, United States Code, provides in relevant part as follows:

> (2) Core proceedings include, but are not limited to--
>
> (A) matters concerning the administration of the estate;
>
> (B) allowance or disallowance of claims against the estate or exemptions from property of the estate, and estimation of claims or interests for the purposes of confirming a plan under chapter 11, 12 or 13 of title 11 . . .

> (N) orders approving the sale of property other than property resulting from claims brought by the estate against the estate; and
>
> (O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims.

28 U.S.C. § 157(b)(2). An action for the imposition of a constructive trust has been described as "akin to a matter concerning the administration of the estate or an adjustment of the debtor-creditor relationship," both of which are examples of core proceedings as defined by the statute. In re Richmond Children's Center, Inc., 49 B.R. 262, 268 (Bankr. S.D.N.Y. 1985), rev'd on other grounds, 58 B.R. 980 (S.D.N.Y. 1986); see also In re Johnson, 960 F.2d 396, 401 n.4 (5th Cir. 1992) ("Various courts have held that actions to impose a constructive trust fall within the definition of core proceedings under the Bankruptcy Code.") (citing cases); cf. In re 400 S. Main St., 133 B.R. 282, 284 (D.R.I. 1991) (adversary proceeding concerning whether debtor was unjustly enriched by payments made by plaintiffs was core proceeding).[18]

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[18]Appellants argue that the bankruptcy court's consideration of the constructive trust claim involved a determination under 28 U.S.C. § 541(a) and (d) about whether the property was or was not part of the debtor's estate, and therefore was a matter of statutory interpretation subject to de novo review. Appellants are correct, as far as it goes, that under section 541(d), property in which the debtor holds only legal title and not an equitable interest -- such as property subject to a constructive trust -- becomes property of the estate "only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that

Because this matter is a core proceedings, this court must apply two different standards of review in passing on the orders of the bankruptcy court. Findings of fact are reviewed under a "clearly erroneous" standard, as provided by Bankruptcy Rule 8013. See In re Howard's Appliance Corp., 874 F.2d 88, 94 (2d Cir. 1989) (reviewing bankruptcy court's findings of fact with respect to constructive trust claim under clearly erroneous standard). As the Supreme Court has explained, a finding is clearly erroneous when "although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." United States v. United States Gypsum Co., 333 U.S. 364, 395 (1948). "Where there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous." Anderson v. City of Bessemer City, N.C., 470 U.S. 564, 574 (1985). Conclusions of law, on the other had, are reviewed on a de novo basis. In re Tesmetges, 47 B.R. 385, 388 (Bankr. E.D.N.Y. 1984).

I.

A. The Constructive Trust Claim

As their primary ground this appeal, H-F an SIN-I argue that the bankruptcy court erred in refusing to impose a constructive trust in their favor on the proceeds from the

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the debtor does not hold." 28 U.S.C. § 541(d); In re Howard's Appliance Corp., 874 F.2d 88, 93 (2d Cir. 1989). However, this conclusion does not undermine the clear holding in the cases cited above that "the only proper forum for determining whether assets held by a debtor are held in constructive trust is the bankruptcy court, and such proceeds must be considered core proceedings." Johns, 960 F.2d at 402.

sale of the property. The parties agree that New York law governs resolution of the constructive trust claim; "[a]s a general rule, the law of the situs of the property, and therefore the trust, governs this determination." However's Appliance Corp., 874 F.2d at 93-94. The bankruptcy court correctly held that a party claiming a constructive trust bears the burden of establishing the existence of the trust relationship. Sonnenschein v. Reliance Ins. Co., 353 F.2d 935, 936-37 (2d Cir. 1965); Caballero v. Anselmo, 759 F. Supp. 144, 147 (S.D.N.Y. 1991) ("Generally, a constructive trust must be proved by plaintiff by clear and convincing evidence.") To be entitled to a constructive trust under New York law, a party generally must establish four elements: (1) a confidential or fiduciary relationship; (2) an express or implied promise; (3) a transfer made in reliance on that promise; and (4) unjust enrichment. In re Koreag, 961 F.2d 341, 352 (2d Cir.), appeal after remand, 1992 WL 200748 (S.D.N.Y. July 31, 1992), cert. denied, ___ U.S. ___, 113 S. Ct. 188 (1992). As this court has observed on another occasion, these four elements are not "talismanic . . . . The New York Court of Appeals has held that the factors may be 'useful,' but that it is possible to have a constructive trust in the absence of a confidential or fiduciary relationship." United States v. Rivieccio, 661 F. Supp. 281, 292, reconsideration denied, 1987 WL 15271 (E.D.N.Y. July 21, 1987) (quoting Simonds v. Simonds, 45 N.Y.2d 233, 241, 380 N.E.2d 189, 194, 408 N.Y.S.2d 359, 363 (1978); see also Koreag, 961 F.2d at 352 ("Although these factors provide important guideposts, the constructive trust doctrine is equitable in nature and should not be 'rigidly limited.'").

In this case, H-F claims that it had a fiduciary relationship with Zinke; that it transferred the $1.5 million to Zinke as an investment in reliance on Zinke's

representations concerning the condominium parking garage; and that Zinke misappropriated the $1.5 million for his own use in purchasing the property. SIN-I, in turn, argues that Zinke violated his fiduciary duty to SIN-I, in turn, argues that Zinke violated his fiduciary duty to SIN-I by drawing the $1.05 million from SIN-I's account and investing it in the Famolare Building. SIN-I further claims that if H-F was repaid its $1.5 million from the proceeds of the Famolare Building, SIN-I's claim should be substituted for or subrogated to H-F's claim against the proceeds. Because SIN-I's claim concededly is dependent upon H-F's claim, this court first will turn to H-F's claim.

1. Was There a Confidential or Fiduciary Relationship?

The bankruptcy court based its finding that "no constructive trust claim can be made out" primarily on H-F's failure, "by any standard," to establish that it stood in a fiduciary relationship with Zinke, or that the $1.5 million transfer was an investment, rather than a loan, to Zinke. The bankruptcy court reached this conclusion based principally upon the "clear and unambiguous" notes -- which were prepared by H-F own counsel -- evidencing the nature of the transaction as a loan. H-F contends that this finding was erroneous and that it has established a common law and/or a statutory fiduciary relationship between H-F and Zinke.

As the bankruptcy court found, the notes indeed reflect a loan to Zinke and Philip Paige -- a corporation of which he was president -- payable on demand, without any restriction on Zinke's use of the funds. By virtue of these notes, H-F and Zinke

> stood in an ordinary, arms-length commercial relationship. Purely commercial transactions do not give rise to a fiduciary relationship. . . . Moreover, "[i]t is a firmly established principle that if a recipient of funds is not prohibited from using them as his own and commingling them with his own monies, a debtor-creditor, not a trust, relationship exists."

Koreag, 961 F.2d at 353.

It bears noting that while the bankruptcy court relied on the parol evidence rule to exclude evidence which H-F and SIN-I sought to introduce to contradict the terms of the two notes, consideration of the excluded evidence would not change the analysis significantly. The prior or contemporaneous evidence that allegedly would vary the terms of the notes consists of the "'Park Place' Condominium Parking Facility Proposal" Zinke provided Fischer; the draft, unsigned joint-venture agreement prepared by Zinke's attorney; and the June 6, 1984 letter Zinke sent to Arthur Young "confirming" that H-F had invested $1.5 million in "a joint venture controlled by our firm named Park Place Associates." Even when taken into consideration, this evidence does not compel a finding that H-F satisfied its burden of proving a confidential relationship. In the first place, there is no evidence in the record to indicate that Zinke previously had made any investments on behalf of H-F, the corporation (Tr. 24); rather, Zinke had an investment relationship with the Plan, which, as Fischer conceded, is an entity separate and distinct from the corporation. (587). Moreover, Fischer's acknowledgement that he never made a demand for the balance of the $1.8 million due on the original $1.5 million note; that notwithstanding H-F's security interest in the Famolare Building, he did not insist that the $1.8 million be

paid out at the closing; and that he never commenced a lawsuit to recover the funds, coupled with the notes -- prepared by H-F's counsel -- that unambiguously reflect a loan transaction, lead this court to affirm Judge Hall's finding that H-F did not establish that it stood in a common law fiduciary relationship with Zinke.

Alternatively, H-F has argued that the bankruptcy court erred in refusing to hold that Zinke was a statutory fiduciary to H-F under the Employee Retirement Income Security Act of 1974 ("ERISA"). H-F bases this argument on Zinke's admission that he was the manager of the Plan in May 1983, and had been an investment advisor for the Plan since approximately 1974; as Zinke testified, "[Fischer] hired my firm to manage his pension fund and gave us discretionary authority with regard to the investment of those firms (sic)." (450).

ERISA defines a fiduciary as follows:

> [A] person is a fiduciary <u>with respect to a plan</u> to the extent (i) that he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, or with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan . . . .

29 U.S.C. § 1002(21) (emphasis added). The term "plan" means "any employee welfare benefit plan or an employee

pension benefit plan or a plan which is both an employee welfare benefit plan and an employee pension benefit plan." 29 U.S.C. § 1002(B)(3).

While the evidence shows that Zinke may have been a fiduciary with respect to the Plan, as Fischer conceded, H-F's pension fund is a "different entity" from H-F, which indisputably is the entity that transferred the $1.5 million to Zinke. (587). In addition, counsel for SIN-I acknowledged at oral argument that "[t]here is no evidence that [Zinke] had ever made an investment for the corporation, only that he had invested for the pension fund." (Tr. 24). Zinke's possible fiduciary relationship with the Plan does not transform him into a fiduciary with respect to H-F for purposes of the ERISA laws. Accordingly, the bankruptcy court correctly found that H-F had failed to establish "by any standard" a fiduciary or confidential relationship with Zinke.

However, the lack of a fiduciary relationship between H-F and Zinke does not necessarily defeat H-F's claim for a constructive trust. Rather, "New York courts have consistently stressed the need to apply the doctrine with sufficient flexibility to prevent unjust enrichment in a wide range of circumstances." Koreag, 961 F.2d at 353. The bankruptcy court therefore should not have ended its analysis at this point, but rather should have considered whether H-F established its entitlement to a constructive trust, notwithstanding the lack of a fiduciary relationship. Accordingly, this court now turns to a review of the other elements governing entitlement to a constructive trust.

2. Was There a Promise, Express or Implied?

The second element of a constructive trust is the making of a promise, whether express or implied. Although the bankruptcy court did not specifically rule on whether or not Zinke expressly or impliedly promised H-F that he would invest the $1.5 million in a condominium parking garage, Judge Hall's finding that the parol evidence rule bars reference to extrinsic evidence contradicting the terms of the notes is relevant to this inquiry, as well.

The notes, which contain no restrictions on Zinke's use of the $1.5 million transferred by H-F, clearly reflect that Zinke did not make an express promise to invest the funds in a parking garage venture. Rather, as the bankruptcy court found and as discussed above, the notes reflect that the parties engaged in a simple loan transaction. Moreover, although it is true that in certain circumstances, a promise may be inferred from the nature of a transaction itself, Brand v. Brand, 811 F.2d 74, 78 (2d Cir. 1987), as the taxing authorities point out, "it is patently unreasonable to believe that H-F's officers and counsel would transfer $1,500,000 to Philip Zinke to purchase real estate without detailing in writing the terms of the agreement and the property to be purchased if this was there (sic) intention." (Gov't Br. at 13-14). Also persuasive is the behavior of H-F subsequent to the transfer; at no time prior to the commencement of these proceedings did H-F demand that the money be returned or assert a legal claim for the funds. See id. at 78-79 (district court properly looked to manner in which parties dealt with property subsequent to transfer). Accordingly, this court concludes that H-F and Sin-I have not proven the existence of an express or implied promise by Zinke.

3. Was There a Transfer Made in Reliance on that Promise?

Although it is undisputed that H-F transferred $1.5 million to Zinke on May 31, 1983, in light of the conclusion reached above that Zinke neither expressly nor impliedly promised H-F that he would invest the $1.5 million in a condominium parking garage, obviously the transfer was not made in reliance on any promise.

4. Was Zinke Unjustly Enriched?

The bankruptcy court concluded that H-F was repaid the $1.5 million it had transferred to Zinke, with interest, out of the proceeds of the refinancing of the Famolare Building. Specifically, the court determined that H-F received $10 million from the refinancing, of which $8.2 million related to the underlying mortgage and $1.8 million related to payment of the notes. (802-03). Based on the evidence adduced at trial, this finding was not clearly erroneous. To the contrary, Zinke testified that the $10 million transfer included the $1.5 million H-F had wired to him on May 31, 1983; and Fischer and Bracken were unable to explain satisfactorily H-F's receipt of approximately $1.8 million over and above the amount due H-F in satisfaction of the mortgage and the equity kicker.[19]

H-F asserts that even if it was repaid the $1.5 million, Zinke and his general creditors nonetheless would be unjustly enriched if they are allowed to retain the proceeds from the sale of the property because the

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[19]Nor was counsel for H-F able to explain clearly what the "equity kicker" implied. E.g., Tr. 50-51.

proceeds would be used in part to pay Zinke's taxes. The New York Court of Appeals has stated that

> [u]njust enrichment...does not require the performance of any wrongful act by the one enriched. Innocent parties may frequently be unjustly enriched. What is required, generally, is that a party hold property "under such circumstances that in equity and good conscience he ought not to retain it."

Simonds, 45 N.Y.2d at 242, 380 N.E.2d at 194, 408 N.Y.S.2d at 364 (quoted in Rivieccio, 661 F. Supp. at 292) (cites omitted). The determination of whether a party has been unjustly enriched involves "a common sense evaluation of the circumstances of the transfer in light of the relationship between the parties, the opportunities for unfairness and overreaching, and equitable principles." Lines v. Bank of Am. Nat'l Trust & Savings Ass'n, 743 F. Supp. 176, 182 (S.D.N.Y. 1990).

In light of the foregoing analysis of the circumstances surrounding H-F's transfer of the $1.5 million to Zinke, this court does not find that either Zinke or the taxing authorities -- as appellants appear to argue -- has been unjustly enriched. Particularly in light of the fact that H-F's counsel prepared the two promissory notes and that all parties involved in the transaction appear to be sophisticated and reasonably well-acquainted with commercial lending practices, equitable principles do not require a finding of unjust enrichment. Therefore, consideration of the elements of a constructive trust apart from the existence of a confidential or fiduciary relationship leads this court to conclude that H-F is not entitled to a

constructive trust on the proceeds from the sale of the property.

B. The Fraud Claim

Appellants argue, alternatively, that Zinke's actual defrauding of H-F obviates the need for them to establish a confidential or fiduciary relationship between H-F and Zinke, or that the transaction was an investment, rather than a loan. The taxing authorities contend -- and appellants have conceded -- that appellants never raised this issue at trial, and that they therefore are precluded from arguing it on appeal; in any event, they contend that appellants cannot establish fraud based on the record presently before the court.

Arguments or issues not raised before a lower court ordinarily cannot be addressed on appeal. Singleton v. Wulff, 428 U.S. 106, 120 (1976). However, "appellate courts -- including district courts sitting as appellate courts in bankruptcy matters -- frequently do address legal arguments raised for the first time on appeal where the argument is clearly presented by the record." In re Ionosphere Clubs, Inc., 114 B.R. 379, 388 (S.D.N.Y.), aff'd in part, rev'd in part, 922 F.2d 985 (2d Cir. 1990), cert. denied, ____ U.S. ____, 112 S. Ct. 50 (1991) (emphasis added); see also In re Hilsen, 119 B.R. 435, 439 (S.D.N.Y. 1990) ("A district court sitting in a bankruptcy appeal has the power to consider any issue presented by the record on appeal, even if the issue was not presented to the bankruptcy court."); In re Monetary Group, 91 B.R. 138, 140 (M.D. Fla. 1988) ("It is within this Court's discretion to resolve an issue not decided in the Bankruptcy Court if the record thoroughly presents the issue.... it is not enough that the record provides facts which may permit the resolution

of an issue; rather, the record must be adequately developed, to the point that the Bankruptcy Court could have passed on the issue, even though that court declined to do so."). Accordingly, even if an argument is not expressly raised before the bankruptcy court, where an argument presents a purely legal issue that does not involve facts outside the record, determination of the issue on appeal may be appropriate. In re Ionosphere, 114 B.R. at 388.

The bankruptcy court made no findings of fact or conclusions of law with respect to the fraud argument. However, while the government is correct that throughout trial and in their post-trial submissions to the bankruptcy court, appellants never argued that Zinke obtained the $1.5 million loan through fraudulent means, the record does contain a number of brief references to a fraud argument by appellants. For example, in the Affidavit of Andrew S. O'Connor, sworn to February 13, 1991, the affiant characterized H-F's claim as follows: "H-F asserts a constructive trust over the Shares by virtue of having been defrauded by Zinke, with the proceeds of Zinke's fraud having been used to purchase the shares." (169). This same characterization appears in an earlier affidavit by O'Connor, sworn to February 16, 1988. (1424). Perhaps more significantly, the parties do not appear to have been completely unaware of appellants' fraud argument: in its pretrial memorandum of law, the United States noted that "Zinke did not use fraud, or questionable means to gain funds for himself which equity and good conscience would not permit him to hold" (Gov't Item 12 at 8); and the debtor, at closing argument before the bankruptcy court, argued that "[n]o evidence, no evidence whatsoever was submitted that there was anything illegal or improper about that transaction." (684). In addition, the taxing authorities have not brought to this court's attention any evidence they

believe should be presented with respect to the fraud claim. Accordingly, the court finds that the record is sufficiently developed with respect to the elements of a claim for common law fraud, and that it is appropriate to rule on appellants' fraud claim even though the bankruptcy court did not do so.

The elements of fraud under New York law include: (1) a material false representation or omission of an existing fact; (2) made with knowledge of its falsity; (3) with intent to defraud; and (4) reasonable reliance; (5) that causes damage to plaintiff. Diduck v. Kaszycki & Sons Contractors, Inc., 974 F.2d 270, 276 (2d Cir. 1992); Morin v. Trupin, 809 F. Supp. 1081, 1095, on reargument, 823 F. Supp. 201 (S.D.N.Y. 1993). In order to succeed on a fraud claim under New York law, the party asserting the claim must prove all these elements by clear and convincing evidence. Leucadia, Inc. v. Reliance Ins. Co., 864 F.2d 964, 971 (2d Cir. 1988), cert. denied, 490 U.S. 1107 (1989); Geler v. National Westminster Bank USA, 770 F. Supp. 210, 212-13 (S.D.N.Y. 1991).

It is necessary for this court to address only the first, fourth and fifth elements of fraud to conclude that appellants have failed to satisfy their burden of proof. First, with respect to the required showing that the party allegedly perpetrating the fraud made a material false representation or omission of an existing fact, Zinke's testimony that he told Fischer he needed immediate access to funds in the event that property became available, and that Fischer advanced the funds to him without restriction as to their use as a personal loan, with the understanding that if a specific deal arose, the deal could be converted into an investment (436-37), is wholly consistent with the documentary evidence produced.

Second, appellants' contention that H-F reasonably relied on Zinke's representations is not supported by the evidence. Rather, the testimony of Fischer and Bracken adduced at trial shows that even after they realized the parking garage venture had been abandoned, H-F did nothing to retrieve the $1.5 million from Zinke. The bankruptcy court's finding that "Mr. Fischer appeared to the Court to be a man who relied heavily upon his own instincts and upon the other officers at Harbison-Fischer, rather than on any definite representations made by Mr. Zinke," (806) is not clearly erroneous and is persuasive in this regard.

Third, in light of this court's affirmance of Judge Hall's finding that H-F was repaid the $1.5 million out of the proceeds of the refinancing of the Famolare Building, it is clear that the record does not support a finding that H-F suffered any damage as a result of the loan transaction. Accordingly, appellants have not established by clear and convincing evidence that Zinke perpetrated a fraud on H-F.

C. SIN-I's Constructive Trust Claim

SIN-I, in turn, claims that it is entitled to a constructive trust on the proceeds from the sale of the property on the ground that Zinke violated his fiduciary duty to SIN-I by borrowing the $1.05 million from SIN-I's account and investing it in the Famolare Building; if H-F was repaid its $1.5 million from the refinancing of the Famolare Building, SIN-I argues, then SIN-I's claim should be substituted for or subrogated to H-F's claim against the proceeds because H-F was paid in part with SIN-I's money.

The bankruptcy court concluded that

> [s]ince Harbison-Fischer cannot establish its claim, the SIN-I Partnership Group claim is also precluded, since its claim is based upon a subrogation to the Harbison-Fischer position. Moreover, the SIN-I Partnership Group claim for constructive trust is premised upon the allegation that SIN-I Partnership Group funds were improperly converted by Philip Zinke, a portion of the proceeds of which ultimately found its way into the Property. No evidence, however, was submitted to the Court to establish that Philip Zinke converted any SIN-I Partnership Group funds.

(804). Addressing first Judge Hall's conclusion that no evidence was submitted establishing that Zinke converted SIN-I's funds, a review of the record indicates that the only evidence submitted by SIN-I in support of its claim included the two checks Zinke wrote on SIN-I's Benham Capital Management Group account, as well as Zinke's testimony that without informing SIN-I, he withdrew the money from the account to invest in the Famolare Building, and that he has not returned the $1.05 million to SIN-I. Notably absent from the record is SIN-I's limited partnership agreement; evidence establishing the actual contractual relationship between Zinke and SIN-I; and evidence establishing that the limited partners of SIN-I were themselves ERISA qualified plans. I therefore agree with the bankruptcy court's conclusion that there was insufficient evidence in the record to support SIN-I's claims that Zinke was an ERISA or common law fiduciary to SIN-I and breached his fiduciary duty to SIN-I by borrowing the $1.05 million from SIN-I's account.

Regarding the bankruptcy court's finding that SIN-I's claim is dependent upon the establishment of H-F's

constructive trust claim, SIN-I now argues that the bankruptcy court should have looked to H-F's entitlement to a constructive trust at the point in time prior to its receipt of the $10 million from the refinancing of the Famolare Building. Specifically, SIN-I contends that even if H-F was repaid the $1.5 million it transferred to Zinke on May 31, 1983, it still had a legitimate constructive trust claim before it was repaid by virtue of Zinke's breach of fiduciary duty or fraud with respect to H-F. However, SIN-I has not disputed that its claim is dependent upon the establishment of a constructive trust by H-F.

As the discussion in the foregoing sections makes clear, H-F has failed to establish that if it had not been repaid, it would have been entitled to a constructive trust on the proceeds from the sale of the property. Rather, H-F's proof on two other elements of its constructive trust claim -- existence of a confidential or fiduciary relationship and an express or implied promise -- was deficient, and its claim would have failed even absent proof that it was repaid the $1.5 million with interest. Similarly, H-F's fraud argument is defeated by the absence of clear and convincing evidence on at least the elements of misrepresentation, reliance and damage.

Accordingly, this court affirms the ruling of the bankruptcy court that SIN-I's constructive trust claim fails as a matter of law.

II.

Appellants also have raised as an issue on this appeal the question of whether the bankruptcy court erred in refusing to enforce a settlement agreement between the debtor, H-F and SIN-I pursuant to which the debtor would

not oppose H-F's and SIN-I's constructive trust claims, and in allowing the debtor to oppose those claims during the trial.

On April 11, 1991, the parties read into the record a stipulation and agreement settling the claims and disputes between the debtor and SIN-I which provided, inter alia, that "[t]his agreement is without prejudice to the rights of Sin I and/or Harvis & Fisher (sic) to pursue its constructive trust claim against the proceeds of sale of the co-op shares relating to 1010 Fifth Avenue, New York, New York. Judith Zinke will cooperate therewith." (220-21). More specifically, the agreement provided as follows:

> Judith Zinke agrees that Harvis & Fisher (sic) and/or Sin I have asserted constructive trust claims and agree to cooperate in the reasonable request of Sin I and Harvis & Fisher (sic) in proof of same.... Judith Zinke does not dispute and will not oppose said constructive trust claims.

(222-23).

The agreement further provided that it was subject to the approval of the courts presiding over the bankruptcies of both SIN-I and the debtor, and that the parties agreed to conclude the settlement and related proceedings "with all due haste." (222) Specifically, "[w]ithin 15 days of this agreement Sin I and Judith Zinke will file all necessary motions for Court approval of this settlement agreement within 15 days of Bankruptcy Court approval of Sin I's participation in this agreement Judith Zinke will file the necessary motions or complaints to complete the transactions outlined ... above." (222). It was agreed that the agreement would be null and void if the

provisions were not met within 120 days "or such further time which shall be agreed on by the parties." (222). The agreement also provided "[f]inally, [that] Judith Zinke shall execute and deliver to Sin I an affidavit of facts regarding the above referenced adversary proceedings satisfactory in form to Sin I." (223). The debtor, who was present at the proceedings, indicated that she understood the agreement and agreed to its terms. (225-26). At the conclusion of the proceedings, Judge Hall remarked "We have this agreement in the record and I understand there will be motions made in this Court for me to approve it[.]" (225).

At a hearing before Judge Hall on July 19, 1991, counsel for the debtor indicated that the settlement had not yet been approved by the court. (363). The court accordingly told counsel that he was "obliged to get involved at this point" in stipulating or objecting to the admissibility of certain documents at trial. (368). The debtor requested that trial be adjourned in light of the fact that the settlement would not be "approved by final order in two weeks under any set of facts," (378), a request to which all parties but the taxing authorities excepted; the court denied the application for an adjournment. (388).

At the commencement of trial on August 5, 1991, counsel for H-F argued that based on the stipulation of settlement, the debtor had no standing to appear in the proceedings. (421-22). The debtor argued that the stipulation was not binding because it never had been approved by Judge Hall or by the bankruptcy court in the SIN-I proceeding; H-F claimed that the delay was due to the debtor's failure to present the agreement to the court for approval. (422). Upon recollecting that he had not approved the agreement at the earlier hearings, Judge Hall permitted the debtor to participate as the plaintiff in the

trial proceedings. (423, 426-27). Judge Hall also denied H-F's motion to introduce the settlement agreement into evidence because "[t]he whole concept had to be approved by the Court and it never was." (668-69).

It is well established that "[a] settlement is a contract, and once entered into is binding and conclusive." Janneh v. GAF Corp., 887 F.2d 432, 436 (2d Cir. 1989), cert. denied, 498 U.S. 865 (1990). However, notwithstanding the fact that the settlement agreement in this case was read into the record on April 11, 1991, the parties do not dispute that the settlement agreement was never submitted to the court for approval; neither SIN-I nor the debtor "file[d] all necessary motions for Court approval" of the agreement, as expressly required by the agreement. Indeed, the parties all concurred with Judge Hall's statement at the conclusion of the proceedings on April 11 that "[w]e have this agreement in the record and I understand there will be motions made in this Court for me to approve it[.]" (225) (emphasis added). Accordingly, an express condition of the settlement contract was not complied with, and, as the bankruptcy court held, the agreement was neither binding nor conclusive.[20]

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[20]I do not agree with the government's argument that the confirmation (in July 1993) of the plan of reorganization, which provided in relevant part that "[o]n confirmation hereof, Debtor will immediately seek to be dismissed as a party to the Constructive Trust Suit, and thereafter, neither Debtor nor her attorney will participate therein in any manner," moots appellants' argument on this issue. Even though the debtor no longer is a party to these proceedings, the question of whether the bankruptcy court properly declined to enforce the settlement agreement and allowed the debtor to participate in the trial is still ripe for consideration on this appeal.

III.

H-F and SIN-I also have raised on this appeal the question of whether the bankruptcy court erred in denying their motion for a new trial. This court affirms Judge Hall's denial of the motion.

Three grounds generally are recognized as a basis for granting a new trial in non-jury cases: (1) manifest errors of law; (2) manifest errors of fact; and (3) newly discovered evidence. Landgray Assocs. v. 450 Lexington Venture, L.P., 1992 WL 147913, at *1 (S.D.N.Y. June 17, 1992), aff'd, 986 F.2d 499 (2d Cir. 1992); Geshwind v. Garrick, 738 F. Supp. 792, 793 (S.D.N.Y. 1990), aff'd, 927 F.2d 594 (2d Cir.), cert. denied, ____ U.S. ____, 112 S. Ct. 58 (1991). In ruling upon motions for a new trial, courts repeatedly have emphasized that Rule 59 is not a substitute for an appeal; "[a] motion under Rule 59 is not intended merely to relitigate old matters already considered or give a disappointed litigant another chance." Agola v. Hagner, 678 F. Supp. 988, 991 (E.D.N.Y. 1987).

As its first ground for moving for a new trial, H-F and SIN-I argued before the bankruptcy court that the misconduct of counsel for the United States in refusing to disclose Zinke's whereabouts gave the United States an unfair advantage and resulted in a "miscarriage of justice." Judge Hall found that these allegations were "devoid of substantive basis." As he noted, H-F and SIN-I failed to specify how they were prejudiced, or to establish any misconduct on the part of the United States. Moreover, Judge Hall found, appellants' failure to object to Zinke's testimony on direct examination clearly precluded their argument on the motion for a new trial. See Simpson v. Standard Oil Co., 223 F.2d 306, 308 (2d Cir. 1955) (refusing

to entertain argument that testimony was admitted erroneously because appellant did not object to admission of testimony when it was offered at trial); Millar Bros. & Co. v. Armour and Co., 149 F. Supp. 661, 661-62 (E.D. Pa. 1957) (defendant could not enlarge objection made at trial on motion for new trial where he did not object to questions eliciting witness's opinion and cross-examined witness about opinion); see also United States v. Sacasas, 381 F.2d 451, 453-54 (2d Cir. 1967) (where witnesses' testimony was not objected to at trial, objection could not be raised on appeal). Accordingly, this court affirms Judge Hall's ruling that there was no miscarriage of justice necessitating a new trial.

Appellants also claimed that the bankruptcy court erred in finding that Zinke was not a statutory fiduciary with respect to both H-F and SIN-I and in refusing to impose a constructive trust. However, as stated above, Rule 59 "is not intended to allow a party 'to relitigate old matters' or to 'present the case under new theories'," IBJ Schroder Bank & Trust Co. v. Resolution Trust Corp., 1993 WL 288266, at *6 (S.D.N.Y. July 23, 1993), and the bankruptcy court properly refused to allow H-F and SIN-I to do so in this case.

Finally, Judge Hall correctly rejected appellants' argument that Zinke's conviction after trial in the Southern District of New York and his cooperation with the government in that action were newly discovered evidence. Newly discovered evidence is ground for a new trial only if the evidence was in existence at the time of trial and could not have been discovered with due diligence by the moving party in time for trial. IBJ Schroder Bank & Trust Co., 1993 WL 288266, at *6; Landgray, 1992 WL 147913, at *5. This court adopts Judge Hall's assessment that "[m]ovants

cannot seriously allege that evidence of convictions and subsequent plea arrangements could not with due diligence have been uncovered in time for trial," (1092), and in any event concludes that the evidence would not be admissible for the purpose of impeaching Zinke. See Fed. R. Evid. 609.

CONCLUSION

In sum, for all the reasons stated above, the September 25, 1991 and December 22, 1992 orders of the bankruptcy court are hereby affirmed in their entirety.

SO ORDERED.

Dated: Brooklyn, New York
February 10, 1994

I. LEO GLASSER, U.S.D.J.

A copy of the foregoing Memorandum and Order were this day sent to:

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The bankruptcy court's opinion on Petitioner's Motion for New Trial is reported at 149 Bankr. Rptr. 310 (E.D.N.Y. 1992). The bankruptcy court denied the Motion for New Trial and no element of the bankruptcy court's denial of the Motion for New Trial is the subject of the Petition to this Court. Therefore, in the interest of brevity and to shorten the documents presented to the Court, the opinion is not reproduced in this Appendix. Petitioner requests leave of Court to omit the opinion from the Appendix.

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NEW YORK

In Re

JUDITH A. ZINKE, a/k/a JUDITH ZINKE, JUDITH ZORN,

Debtor

JUDITH A. ZINKE,

Plaintiff,

-against-

UNITED STATES DEPARTMENT OF THE TREASURY; NEW YORK STATE TAX COMMISSION; CITY OF NEW YORK DEPARTMENT OF FINANCE; SHERMAN, CITRON & KARASIK; DEJET SYSTEMS; DENWELL CONTRACTORS, INC.; GOODMAN PLUMBING AND HEATING CORP.; ROBERT ABRUSSO; STRAZZEN & SON; ENVIRONMENTAL CONTROL BOARD; V.A. PARADISE, as Trustee for Schiavone Construction Company Profit Sharing Plan and Schiavone Construction Company Pension Trust; PHILIP ZINKE, JOHN DOES and JANE DOES, being individuals, partnerships, corporation or other entities whose real names are unknown, who may have an interest in the property to be sold,

Defendants.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

A trial having been held on August 5, 1991, and August 6, 1991, to consider the claims of Harbison-Fischer Manufacturing Co., Inc. ("Harbison-Fischer"), and the SIN-I Partnership and its general and limited partners, including, but not limited to, V.A. Paradise, as Trustee for Schiavone Construction Company Profit Sharing Plan, Schiavone Construction Company Pension Trust and Irwin K. Kline and Joseph H. Cooper, as Trustees for Lankenau Pathology Associates, Inc. Profit Sharing Trust (collectively referred to as the "SIN-I Partnership Group"), against a certain cooperative apartment located at 1010 Fifth Avenue, New York, New York (the "Property") and/or its proceeds ("Proceeds"), and after due consideration of the evidence and the memorandum of law submitted, and for the reasons more particularly stated on the record at the August 5, 1991 hearing, and in these findings of facts and conclusions of law, the Court having determined that Harbison-Fischer and the SIN-I Partnership Group have not met their burden in establishing a constructive trust and therefore have no claims against the Property or its Proceeds, it is determined as follows:

PROCEDURAL BACKGROUND

1. On September 29, 1987, the Debtor, Judith Zinke, filed a petition seeking an order of relief under the protective provisions of Chapter 11 of the Bankruptcy Code.

2. On November 3, 1987, the Debtor commenced these adversary proceedings seeking to sell the Property free and clear of all liens, encumbrances and claims, with the proceeds to be used to, among other things,

satisfy tax liens asserted by the United States Department of Treasury and the New York State Department Taxation and Finance ("Tax Liens"). The Debtor also sought declaratory determination that no other parties had a claim in the Property or its proceeds.

3. On December 2, 1987, an order was entered

(a) authorizing the sale of the Property, free an clear of all liens, encumbrances and claims;

(b) authorizing the satisfaction of the Tax Liens without prejudice; and

(c) reserving jurisdiction with respect to the claims of Harbison-Fischer and the SIN-I Partnership Group to an alleged constructive trust in the Property and/or its Proceeds ("Constructive Trust Claim").

4. Except with regard to the claims of Harbison-Fischer and the SIN-I Partnership Group, no other party has made any claim to the Property or its Proceeds.

5. The gravamen of the Constructive Trust Claim is that on or about May 31, 1983, Harbison-Fischer wired $1.5 million dollars to Philip Zinke, the Debtor's husband, from which a portion of the $1.5 million dollars was used to purchase the Property. Concededly, the SIN-I Partnership Group's claim for a constructive trust is dependent upon the establishment of Harbison-Fischer's constructive trust claim. If the Harbison-Fischer constructive trust claim is unenforceable, the SIN-I

Partnership Group's claim falls as a matter of law, since their claim is based upon subrogation rights.

FINDINGS OF FACT

The Court finds as follows:

1. The $1.5 million dollar advance by Harbison-Fischer was an interest-bearing loan ("$1.5 Million Dollar Loan"). The $1.5 Million Dollar Loan was evidenced by two (2) promissory notes prepared by Harbison-Fischer's counsel, the first Note in the original amount of $1.5 million dollars, dated May 31, 1983, bearing interest at prime, and a second updated note of October 3, 1984, in which $253,868.44 of interest was added to the original $1.5 million dollar principal loan balance (collectively referred to as the "Notes"). No restriction of any nature was placed on Philip Zinke's use of the proceeds of the $1.5 Million Dollar Loan. The Notes are clear and unambiguous on their face, evidencing a loan transaction. See also the Harbison-Fischer demand letter dated December 3, 1984, requesting payment on the $1.5 Million Dollar Loan, inclusive of interest, totalling $1,790,452.24.

2. The original $1.5 Million Dollar Loan obligation was repaid in full, inclusive of interest, out of the proceeds of a refinancing with respect to a certain property owned by Philip Zinke, located on 4 East 54th Street, New York, New York ("54th Street Property"). From the refinancing of the 54th Street Property, Harbison-Fischer received $10 million dollars of which approximately $8.2 million dollars related to the underlying mortgage held by Harbison-Fischer against the 54th Street Property with the $1.8 million dollar balance paid in satisfaction of the Notes. (*see Addendum A for Supplemental Findings of Fact.)

CONCLUSIONS OF LAW

1. It is well-settled that ordinary contractual relationships do not rise to the level of a fiduciary duty. To impress a constructive trust, there must be at least a wrongdoing greater than the non-payment of a debt. McKey v. Paradise, 299 U.S. 119 (1936); accord, In re Penn Dixie Steel Corp., 6 B.R. 817, 823-824 (Bankr. S.D.N.Y. 1980); aff'd, 10 B.R. 878 (S.D.N.Y. 1981); In re Richmond Children's Center, Inc., 49 B.R. 262 (Bankr. S.D.N.Y. 1985). In the present case, the facts indicate a loan transaction, which, in fact, was repaid. Finding of fact numbers 1 and 2. Consequently, no constructive trust claim can be made out.

2. Additionally, since the Notes evidencing the $1.5 Million Dollar Loan were prepared by Harbison-Fischer's counsel, and are clear and unambiguous on their face, any evidence which Harbison-Fischer or the other defendants say seek to interpose to contradict the terms of the Notes evidencing merely a loan arrangement, would be barred under the Parole Evidence Rule. Maloney v. Weingarten, 500 N.Y.S. 2d 320 (A.D. 2 Dept. 1986), lv. to app. den., 516 N.Y.S. 2d 1023 (1986); accord, Obaydon v. Ujvari v. Loney, (A.D. 1 Dept. 1989); Lebowitz v. Mingus, 474 N.Y.S. 2d 748 (A.D. 1 Dept. 1984).

3. Since Harbison-Fischer cannot establish its claim, the SIN-I Partnership Group claim is also precluded, since its claim is based upon a subrogation to the Harbison-Fischer position. Moreover, the SIN-I Partnership Group claim for constructive trust is premised upon the allegation that SIN-I Partnership Group funds were improperly converted by Philip Zinke, a portion of the proceeds of which ultimately found its way into the Property. No evidence, however, was submitted to the Court to establish

that Philip Zinke converted any SIN-I Partnership Group funds. Since the burden of proof is on Harbison-Fischer and the SIN-I Partnership Group, their failure to meet such burden bars any claim against the Property or its proceeds.

4. The claims of Harbison-Fischer and the SIN-I Partnership Group, or any other defendant, as against the Debtor, the United States Department of the Treasury, the New York State Tax Commission, the Property or its Proceeds are dismissed with prejudice.

SO ORDERED:

Dated: Westbury, New York
September 25, 1991

BANKRUPTCY JUDGE
Robert John Hall

ADDENDUM A
SUPPLEMENTAL FINDINGS OF FACT

In their Findings of Fact, the SIN-I Partnership and Harbison-Fischer Manufacturing Co., Inc. ask the Court to evaluate the credibility of the witnesses.

(3) In listening to Charles Fischer, it was the impression of the Court that although Mr. Fischer was trying to be direct and forthright, he was unable to justify or substantiate many of his own impressions and conclusions. Mr. Fischer appeared to the Court to be a man who relied heavily upon his own instincts and upon the other officers at Harbison-Fischer, rather than on any definite representations made by Mr. Zinke. Much of Mr. Fischer's testimony was vague.

(4) The documents prepared by the counsel for Harbison-Fischer treated the transaction as a loan, with Mr. Zinke being personally liable to repay the monies, and with no limitation on the use of the monies. These notes contradict the investment theory urged by Harbison-Fischer.

(5) The inaction of Harbison-Fischer until the notice of sale confirms that the transaction was a loan and not an investment.

(6) Harbison-Fischer has the burden of proof, and has failed to establish by any standard, a fiduciary or confidential relationship or that the transaction was an investment.

(7) The loan documents support Mr. Zinke's testimony and the Court did not hear anything or see anything which would demonstrate that Mr. Zinke's testimony was not credible.

(3)

Supreme Court, U.S.
FILED
OCT 23 1995
CLERK

No. 95-301

In the Supreme Court of the United States

OCTOBER TERM, 1995

STONEHENGE INSURED NOTES-I LIMITED PARTNERSHIP, ET AL., PETITIONERS

v.

UNITED STATES DEPARTMENT OF THE TREASURY, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENTS IN OPPOSITION

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QUESTION PRESENTED

Whether the courts below correctly declined to impose a constructive trust in favor of petitioners on proceeds from the sale of an apartment by a debtor in bankruptcy.

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OPINIONS BELOW

The opinion of the court of appeals (Pet App. B1-B7) is unpublished, but the decision is noted at 47 F.3d 1157 (Table). The opinions of the district court (Pet. App. D1-D41) and the bankruptcy court (Pet. App. F1-F7) are unreported. Related opinions of the bankruptcy court are reported at 157 B.R. 528, 149 B.R. 310, and 97 B.R. 155.

JURISDICTION

The judgment of the court of appeals was entered on January 10, 1995. A petition for rehearing was denied on May 19, 1995. Pet. App. A1-A2. The petition for a

writ of certiorari was filed on August 17, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. In May 1983, after some discussion of a possible investment in a New York City parking garage, petitioner Harbison-Fischer Mfg. Co., Inc. (HF) wired $1.5 million of corporate funds to the order of Philip Zinke. Although Zinke was the manager of HF's retirement plan, the wired funds belonged to the corporation, not to the plan. The funds were deposited in an account in the name of an association of which Zinke was president, and the next day $810,000 was transferred from that account to an account in the name of a corporation of which Zinke was also president. A check for $810,000 was drawn on that corporation's account and delivered as partial payment for the purchase, by Zinke and his wife, of a cooperative apartment at 1010 Fifth Avenue in New York City. Pet. App. D4, D6.

Petitioner Stonehenge Insured Notes-I Limited Partnership (Stonehenge) is a limited partnership of which Zinke was the general partner. In April and July 1984, Zinke drew two checks on Stonehenge's account for a total of $1.05 million, which he used as partial payment for the acquisition of a building in midtown Manhattan (the Famolare building). Pet. App. D5. In August 1984, HF, through Zinke, provided an additional $7.9 million for the purchase of the Famolare building, through a loan secured by a mortgage on the building. The loan and mortgage contained an "equity kicker"—that is, a provision giving HF, in addition to stated interest on the loan

amount, a share in any appreciation realized on the property's resale. Pet. App. D5; see C.A. App. 301-302.

Zinke executed two notes to HF that were prepared by HF's counsel: one dated as of May 31, 1983, for $1.5 million, and one dated as of October 1, 1984, for $1,753,868.44 (reflecting interest accrued on the $1.5 million from May, 1983). Pet. App. D7; see *id.* at D10. The second note was secured by an interest in the Famolare building. *Id.* at D7. In December 1984, HF sent Zinke a letter requesting payment of principal and interest totalling $1,790,452.24. *Id.* at D8.

In January 1985, Zinke arranged to refinance the Famolare building. HF received approximately $10 million in that transaction, including repayment of approximately $8.2 million in principal and interest then due on its secured loan. Pet. App. D8, D10-D12, D14. The refinancing agreement specifically provided that HF would retain its interest in any appreciation in the building's value, which therefore could not account for the additional $1.8 million that HF received. See *id.* at D10-D12. After the refinancing, HF made no further demand for the $1.8 million balance previously due on the Zinke notes. *Id.* at D11-D12.

2. Zinke's wife filed for bankruptcy in September 1987 and then commenced this adversary proceeding, seeking an order allowing her to sell the Fifth Avenue apartment free and clear of other claims and to use the proceeds to satisfy, among other things, federal and state tax liens. Pet. App. B3. HF and Stonehenge objected, each seeking to have the bankruptcy court impose a constructive trust in its favor against the proceeds from sale of the apartment. *Ibid.* HF claimed that Zinke had misappropriated the $810,000 of its funds that he used to purchase the

apartment, thereby breaching an alleged fiduciary duty. See *id.* at D21-D22, F3. Stonehenge, in turn, claimed that Zinke violated a fiduciary duty owed to it when he used $1.05 million of its funds to purchase the Famolare Building. *Id.* at D22. Although Stonehenge's funds were not used to acquire the Zinke apartment, Stonehenge argued that if HF's $1.5 million was repaid out of the proceeds of refinancing the Famolare Building, then Stonehenge's claim should be "substituted for or subrogated to HF's claim against the proceeds" from the apartment's sale. *Ibid.*; see *id.* at F3-F4.

The bankruptcy court rejected petitioners' claims. Pet. App. F1-F6. The court concluded that the $1.5 million advance from HF to Zinke was an ordinary commercial loan, evidenced by promissory notes prepared by HF's own counsel and ultimately repaid in full out of the proceeds from the refinancing of the Famolare building. *Id.* at F4, F7. On those facts, the court found that HF had failed to establish either a fiduciary relationship between it and Zinke, or any entitlement to the imposition of a constructive trust. *Id.* at F5, F7. Because Stonehenge's claim was based entirely on "subrogation" to HF's position, the failure of HF's claim also precluded recovery by Stonehenge. *Id.* at F5. In addition, the court noted that Stonehenge had failed to submit any evidence that Zinke had improperly converted any of its partnership funds. *Id.* at F5-F6.[1]

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[1] Zinke maintained that he had executed promissory notes relating to the $1.05 withdrawn from SIN-I's accounts, and that the SIN-I partnership agreement gave him the right to undertake such a transaction. See C.A. App. 297, 318-321; see also Pet. App. D5 n.5. As petitioners note (Pet. 5 n.1; see Pet. App. D5 n.5), Zinke was separately charged with grand

3. The district court affirmed. Pet. App. D1-D40. After a detailed review of the record (*id.* at D2-D17), the court agreed that the evidence supported treating the $1.5 million transfer from HF to Zinke as an ordinary loan transaction, and that HF "did not establish that it stood in a common law fiduciary relationship with Zinke." *Id.* at D24. The court also rejected (*id.* at D24-D25) HF's contention that Zinke was a "statutory fiduciary" to HF under the Employee Retirement Income Security Act of 1974 (ERISA). Acknowledging that Zinke might have been a fiduciary with respect to the HF retirement plan, which he managed, the court pointed out that the company and the plan were different entities, that the loan came from the company, and that "Zinke's possible fiduciary relationship with the Plan does not transform him into a fiduciary with respect to [HF] for purposes of * * * ERISA." Pet. App. D25.

The district court also concluded (Pet. App. D26-D29) that HF had failed to establish any other element that might have supported the imposition of a constructive trust. Because Zinke had unrestricted use of the funds, the court found no promise by Zinke to invest them on HF's behalf, nor any reliance upon such a representation in making the transfer. *Id.* at D26-D27. And because HF was repaid in full out of the proceeds of the Famolare building refinancing, there could be no finding that Zinke had been unjustly enriched by the loan transaction. *Id.* at D27-D28.

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larceny in connection with the diversion of the $1.05 million. His conviction was overturned on appeal on the ground that, as a matter of law, "in New York, partners cannot be charged with larceny for misappropriating firm assets." *People* v. *Zinke*, 556 N.Y.S.2d 11, 14 (1990), rev'g 146 A.D. 106 (1st Dep't 1989).

The district court similarly upheld the bankruptcy court's rejection of Stonehenge's constructive trust claim. Pet. App. D32-D34. In the absence of any record evidence concerning the Stonehenge limited partnership agreement, any other contractual relationship between Zinke and Stonehenge, or whether some or all of Stonehenge's limited partners were ERISA plans, the court "agree[d] with the bankruptcy court's conclusion that there was insufficient evidence in the record to support [Stonehenge's] claims that Zinke was an ERISA or common law fiduciary to [Stonehenge] and breached his fiduciary duty to [Stonehenge] by borrowing the $1.05 million from [Stonehenge's] account." *Id.* at D33. Moreover, the court noted that Stonehenge "has not disputed that its claim is dependent upon the establishment of a constructive trust by HF" (*id.* at D34), so that the rejection of HF's claims necessarily entailed the failure of Stonehenge's claim as well. *Ibid.*[2]

4. The court of appeals affirmed. Pet. App. B1-B7. The court found no clear error in the bankruptcy court's findings that the $1,500,000 transfer from HF to Zinke was a loan and that the loan was fully repaid, with interest, from the proceeds of refinancing the Famolare building. *Id.* at B4-B5. On the basis of those findings, the court of appeals affirmed the lower courts' holdings that petitioners "failed to prove

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[2] The district court also considered and rejected arguments that Zinke had defrauded HF (Pet. App. D29-D32), that the bankruptcy court had erred by refusing to enforce a settlement agreement under which Zinke's wife (the debtor) had purportedly agreed not to contest the constructive trust claims (*id.* at D34-D37), and that the bankruptcy court should have granted petitioners' motion for a new trial (*id.* at D38-D40). Petitioners do not renew those arguments in this Court.

either a fiduciary relationship or unjust enrichment," and concluded that "neither [lower] court abused its discretion in declining to impose a constructive trust" in favor of HF. *Id.* at B5. The court also rejected Stonehenge's claim. *Id.* at B5-B6. Because the partnership could not trace its funds to the Fifth Avenue apartment, its claim derived from and depended on HF's claim (*ibid.*); and because "[HF] failed to secure a constructive trust in its favor, [Stonehenge's] claim fails as well" (*id.* at B6).[3]

ARGUMENT

1. Petitioners purport to present five questions involving the Employee Retirement Income Security Act of 1974. Pet. i. Those questions, however, have little to do with the facts of this case as found by the lower courts. As the courts below uniformly concluded, Philip Zinke borrowed money from petitioner HF, a commercially sophisticated corporation with which he had no fiduciary relationship. Pet. App. B3-B4, D22-D25, D28, F4-F5. Zinke used some of that money to buy an apartment. *Id.* at B3. He later repaid the loan, using proceeds from the refinancing of a building in which he held an equity interest. *Id.* at B4-B5. That interest was acquired in part with funds that Zinke obtained, under unclear circumstances (see *id.* at D5 & n.5), from petitioner Stonehenge, of which he was the general partner. That sequence of events raises squarely the common-law questions of fiduciary duty, misappropriation, and constructive trust that were considered and resolved by the courts below. It raises no issue under ERISA.

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[3] The court of appeals also rejected petitioners' claim that they were entitled to a new trial. Pet. App. B6-B7.

Petitioners attempt to bring their claims within the purview of ERISA by alleging (i) that Zinke was the investment manager of petitioner HF's pension plan (Pet. 6) and (ii) that the HF plan "and other pension plans" were limited partners in petitioner Stonehenge (Pet. 6, 11). As the courts below correctly held, however, the first point is irrelevant, because whatever relationship Zinke had with HF's pension plan did not make him an ERISA fiduciary of the company itself, and it was from the company that he borrowed the money used to purchase his apartment. Pet. App. B3-B4, D24-D25.

With respect to the second point, the district court reviewed the record and found that Stonehenge had failed to produce a copy of its own limited partnership agreement, any other evidence of the contractual relationship between the partnership and Zinke, or any evidence establishing that the limited partners were plans covered by ERISA.[4] Pet. App. D33. Under the circumstances, the courts below were fully justified in rejecting (*id.* at D24-D25, D33) petitioners' attempt to characterize Zinke as an ERISA fiduciary with respect to either HF or Stonehenge. That fact-bound determination warrants no further review, and its acceptance leaves no basis in the record for consideration of the questions that petitioners ask this Court to resolve.[5]

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[4] Petitioners offer no citation for their assertion (Pet. 11) of an "admission by Zinke that he was an ERISA fiduciary to * * * pension plans that were limited partners of Stonehenge." Compare Pet. App. D33.

[5] Petitioners argue (Pet. 12-14) that even if Zinke was not a fiduciary of HF, he could be liable "as a party-in-interest and a non-fiduciary for knowing participation in a breach of his [own] fiduciary duties with respect to Stonehenge funds." Pet. 14.

2. The court of appeals correctly upheld the lower courts' conclusion that petitioners failed to establish their entitlement to a constructive trust. The evidence reviewed by the bankruptcy court (Pet. App. F4-F6) and the district court (*id.* at D22-D24, D27), including the loan documents prepared by HF's own attorneys and the financial details of the Famolare building refinancing, amply supported the courts' findings that the transfer of the $1.5 million to Zinke and the additional cash transmitted to HF as part of the refinancing represented the routine making and repayment of a loan between commercially sophisticated parties. Compare, *e.g.*, *Brand* v. *Brand*, 811 F.2d 74, 77 (2d Cir. 1987) (fiduciary relationship and unjust enrichment generally prerequisite to imposition of constructive trust).

Similarly, the courts below properly rejected petitioner Stonehenge's attempt to impose a constructive trust on proceeds from the sale of the Fifth Avenue apartment. New York law requires that a party trace his property into any property or fund on which he seeks to impose a constructive trust. Pet. App. B5; see, *e.g.*, *Fur & Wool Trading Co.* v. *George I. Fox, Inc.*, 156 N.E. 670, 671 (N.Y. 1927). Stonehenge could trace its funds to the Famolare building (Pet. App. 5),

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As discussed above, the courts below properly held that the record in this case would not support a finding that Zinke was a fiduciary with respect to Stonehenge *or* HF. Moreover, the Court recently declined to address the question of a non-fiduciary's liability for knowing participation in the violation of fiduciary duties under ERISA. *Reich* v. *Continental Casualty Co.*, 115 S. Ct. 1104 (1995). Even if the question were properly presented, there would be no reason for a different result here.

not to the Zinke apartment.[6] And even if Stonehenge were able to frame a valid theory of "subrogation" to any claim that HF might have had against Zinke, it conceded below that such a claim would fail if HF itself could not recover. See C.A. App. 349; Pet. App. B5-B6, D33-D34. The courts below were entitled to rely on that concession. Compare Pet. 9-10.

Finally, there is no merit to petitioners' contention (Pet. 14-16) that the courts below erroneously required them to prove the existence of a fiduciary relationship. As petitioners conceded at trial (C.A. App. 251-252), the party seeking to establish a constructive trust in New York bears the burden of proving the existence of the underlying fiduciary relationship. Pet. App. D21; see, *e.g.*, *Cabellero* v. *Anselmo*, 759 F. Supp. 144, 147 (S.D.N.Y. 1991). Even if we assume that they are relevant here, none of the cases cited by petitioners involving ERISA fiduciaries holds to the contrary. See *Leigh* v. *Engle*, 727 F.2d 113, 138 (7th Cir. 1984) (defendants found to have breached fiduciary duties bore burden of separating profits from improperly commingled assets); *Whitfield* v. *Lindemann*, 853 F.2d 1298, 1305 (5th Cir. 1988) (assuming, without deciding, that defendants should bear burden of proving that a breach of duty did not cause loss), cert. denied, 490 U.S. 1089 (1989); *Donovan* v. *Cunningham*, 716 F.2d 1455, 1467-1468 & n.27 (5th Cir. 1983) (fiduciaries of employee stock ownership plan required to show they paid a fair price for securities purchased from

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[6] Petitioners' assertion (Pet. 11) that some of Stonehenge's funds were used to purchase the apartment has no foundation in the record.

employer), cert. denied, 467 U.S. 1251 (1984).[7] Petitioners cite no case in which a court required a defendant to prove that he was not a fiduciary.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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[7] Petitioners also cite (Pet. 15-16) three earlier decisions rendered by the court below. The decision in this case does not conflict with any of those decisions. In *New York State Teamsters Council* v. *Estate of DePerno*, 18 F.3d 179, 180 (2d Cir. 1994), for example, the court required the plaintiffs to establish the defendants' violation of a fiduciary duty to an ERISA plan, before the burden shifted to the defendants to show factors mitigating damages. Even if the decisionswere in conflict, however, the matter would be one for resolution by the court of appeals itself. See *Wisniewski* v. *United States*, 353 U.S. 901, 902 (1957).